DOCKET

(23)

No. 86-1970-ASX
Status: GRANTED

Docketed:
June 10, 1987

Title: Mississippi Power & Light Company, Appellant
v.
Mississippi ex rel. Michael C. Moore, Attorney General of Mississippi, and Mississippi Legal Services Coalition

Court: Supreme Court of Mississippi

Counsel for appellant: Lee,Rex

Counsel for appellee: Maxey II,John L., Pennington,Jesse C., Wise,Richard W.

NOTE* Notice of Appeal filed 5/20/87

Entry	Date	Note	Proceedings and Orders
3	May 21 1987		Application for stay filed (A-846) and referred to the Court by Justice White on May 22, 1987.
6	May 21 1987		Above application for stay granted by order of the Court on June 1, 1987.
4	May 22 1987		Above application DISTRIBUTED for May 28, 1987. Responsefiled on May 26, 1987.
5	May 27 1987		Response of Mississippi Publice Service Commission to A-846 filed on May 27, 1987. Reply brief filed 5/27/87.
1	Jun 10 1987	G	Statement as to jurisdiction filed.
2	Jun 10 1987		Appendix of appellant MS Power & Light Co. filed.
7	Jun 22 1987		Application for stay filed (A-936).
8	Jun 23 1987		Responses to above application filed by MS Legal Servs. Coalition, State of MS, etc. and MS Public Serv.
9	Jun 23 1987		Commn.
10	Jun 23 1987		The above application referred to the Court by White, J.
11	Jun 23 1987		The application for stay of the Order Granting Mandatory Temporary Restraining Order and Setting Aside Chancery
12	Jun 23 1987		Court Order of June 18, 1987, issued by the Supreme Court of Mississippi on June 19, 1987, presented to Justice
13	Jun 23 1987		White and by him referred to the Court, is hereby GRANTED pending further order of the Court.
15	Jul 1 1987		Order extending time to file response to jurisdictional statement until August 10, 1987.
16	Jul 1 1987		The above extension applies to all appellees.
20	Jul 29 1987		Brief amici curiae of United States, et al. filed.
22	Aug 7 1987		Brief amicus curiae of Edison Electric Institute filed.
21	Aug 10 1987		Motion of appellees MS Legal Services Coalition to dismiss filed.
23	Aug 10 1987		Brief amicus curiae of New Orleans filed.
24	Aug 10 1987		Brief amici curiae of Arkansas Public Service, et al. filed.
25	Aug 10 1987		Motion of appellees Mississippi, et al. and appendix to dismiss filed.
26	Aug 12 1987		DISTRIBUTED. September 28, 1987
27	Aug 25 1987	X	Reply brief of appellant MS Power & Light Co. filed.
28	Oct 5 1987		Further consideration of the question of jurisdiction is POSTPONED to the hearing of the case on the merits.

****

2 PP

No. 86-1970-ASX

Entry	Date	Note	Proceedings and Orders
30	Oct 19 1987		Order extending time to file brief of appellant on the merits until December 3, 1987.
31	Nov 15 1987		Record filed.
		*	Certified copy of original record received on 11/15, 11/16, 11/17 & 11/18. 33 volumes.
32	Dec 3 1987		Brief amici curiae of United States, et al. filed.
33	Dec 3 1987		Brief amicus curiae of Edison Electric Institute filed.
34	Dec 3 1987		Joint appendix filed.
35	Dec 3 1987		Brief of appellant MS Power & Light Co. filed.
37	Dec 10 1987		Order extending time to file brief of appellee on the merits until January 22, 1988.
38	Dec 11 1987	G	Motion of the Solicitor General for leave to participate in oral argument as amici curiae and for divided argument filed.
39	Jan 5 1988		SET FOR ARGUMENT. Monday, February 22, 1988. (1st case).
40	Jan 5 1988		CIRCULATED.
41	Jan 11 1988		Motion of the Solicitor General for leave to participate in oral argument as amici curiae and for divided argument GRANTED.
42	Jan 22 1988	X	Brief amici curiae of Consumer Federation of America, et al. filed.
43	Jan 22 1988	X	Brief amici curiae of Arkansas Public Service, et al filed.
44	Jan 22 1988	X	Brief of appellee Mississippi filed.
45	Jan 22 1988	X	Brief of appellee Mississippi Legal Services Coalition filed.
46	Jan 22 1988	X	Brief amicus curiae of Council of the City of New Orleans filed.
47	Jan 22 1988	X	Brief amici curiae of National Governors' Association, et al. filed.
48	Jan 22 1988	X	Brief amicus curiae of Natl. Assn. of State Utility Consumer Advocates filed.
49	Feb 8 1988	X	Reply brief of appellant MS Power & Light Co. filed.
50	Feb 22 1988		ARGUED.

JURISDICTIONAL

STATEMENT

86 1970 (1)

No. 86-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

JURISDICTIONAL STATEMENT

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi
39205
(601) 354-2385

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 331-9400

Of Counsel:
WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

Attorneys for Appellant

**Counsel of Record*

28 pp

QUESTION PRESENTED

This case presents the same question under the Federal Power Act and the Commerce Clause that the Court decided last term in *Nantahala Power & Light Company* v. *Thornburg*, No. 85-668, 106 S. Ct. 2349 (1986):

> Whether a state regulatory commission may nullify a FERC wholesale rate decision that allocates the wholesale costs of generating electricity among affiliated electric utilities that serve different states?

PARTIES BELOW

The appellants below were the State of Mississippi ex rel. Edwin Lloyd Pittman, Attorney General of Mississippi, and the Mississippi Legal Services Coalition.

The Appellees were Mississippi Power & Light Company, Mississippi Resident Security Owners, and the Mississippi Public Service Commission.

RULE 28.1 STATEMENT

Mississippi Power & Light Company ("MP&L")is a wholly-owned subsidiary of Middle South Utilities, Inc. Middle South Utilities, Inc. has no parent company. Its other wholly-owned subsidiaries are Arkansas Power & Light Company ("AP&L"), Louisiana Power & Light Company ("LP&L"), New Orleans Public Service Inc. ("NOPSI"), System Energy Resources, Inc. (formerly named Middle South Energy, Inc.), MSU System Services, Inc. (formerly named Middle South Services, Inc.), and Electec, Inc. In addition, AP&L, LP&L, MP&L, and NOPSI jointly own the common stock of System Fuels, Inc., and AP&L owns the common stock of Associated Natural Gas Company.

TABLE OF CONTENTS

[1]The Appendix to the Jurisdictional Statement ("App.") has been separately bound, pursuant to Rule 15(j).

TABLE OF AUTHORITIES

Administrative Decisions

Statutes

No. 86-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

JURISDICTIONAL STATEMENT

OPINIONS BELOW

The opinion of the Supreme Court of Mississippi, dated February 25, 1987 (App. 1a-23a), and its decision denying rehearing, dated May 20, 1987 (App. 197a-198a), are not yet reported. The Final Order on Rehearing of the Mississippi Public Service Commission, dated September 16, 1985 (App. 25a-59a) is unreported. In addition, the decisions of the Federal Energy Regulatory Commission ("FERC") that establish the wholesale power and cost allocations and rates that are at issue in this appeal are reproduced in the Appendix: FERC Opinion No. 234 (App. 73a-152a), which is reported at 31 FERC (CCH) ¶ 61,305 (1985), and FERC Opinion No. 234-A (App. 153a-195a), which is reported at 32 FERC (CCH) ¶ 61,425 (1985).

JURISDICTION

The judgment of the Mississippi Supreme Court rejecting appellant's constitutional challenge to a Mississippi statute, *Miss. Code Ann.* § 77-3-39 (Supp. 1986), was issued February 25, 1987. MP&L's timely petition for rehearing was denied on May 20, 1987. MP&L filed a Notice of Appeal on May 20, 1987. App. 201a-202a. This Court has jurisdiction under 28 U.S.C. § 1257(2). *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986) ("*Nantahala I*"); *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-1307, 106 S. Ct. 3268 (June 23, 1986) ("*Nantahala III*").[2]

CONSTITUTIONAL AND STATUTORY PROVISIONS

The United States Constitution, Article VI, Clause 2: "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land . . . ."

The United States Constitution, Article I, Section 8, Clause 3: "The Congress shall have Power . . . [t]o regulate Commerce . . . among the several States . . . ."

The pertinent provisions of the Federal Power Act, 16 U.S.C. §§ 791a-828c, and of the Mississippi Code, §§ 77-3-37, 77-3-39, are reprinted at pages 61a-68a and 69a-71a, respectively, of the Appendix to the Jurisdictional Statement.

[2]In this case, as in *Nantahala III*, a state supreme court set aside a utility commission order that gave effect to FERC rate schedules, and the state supreme court rejected arguments that federal law preempted a state statute that required the state commission to investigate the prudence of expenses incurred under FERC regulation. In this circumstance, there is a "final judgment" within the meaning of 28 U.S.C. § 1257. Because the Mississippi Supreme Court "has finally determined the federal issue[s] present in [this] case," this Court's decisions make it very clear that appellants need not spend years re-litigating the appropriate interstate cost and power supply allocations before the Mississippi Public Service Commission and other Mississippi tribunals before appellants may come to this Court and seek to have the original state commission order reinstated. *See Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 476-87 (1975).

STATEMENT OF THE CASE

Introduction

This case presents the same question that the Court decided last term in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986): whether a single state regulatory commission may nullify a FERC wholesale rate decision that allocates the wholesale costs of generating electricity among affiliated electric utilities that serve different states. In *Nantahala*, this Court unequivocally prohibited such collateral attacks on FERC's regulation. The Court held that state utility commissions are bound by FERC's interstate wholesale cost allocations and must treat FERC-approved costs as reasonable operating expenses in setting retail rates.

In this case, however, the Mississippi Supreme Court held that its state commission can disregard FERC's cost allocations if found "excessive" or "imprudent" and may set retail rates on the basis of the very interstate cost allocations that Mississippi unsuccessfully urged FERC to adopt—all in direct conflict with *Nantahala*. The Mississippi Supreme Court's holding also directly conflicts with a recent decision of the Fourth Circuit, *Appalachian Power Co.* v. *Public Service Commission of West Virginia*, 812 F.2d 898 (4th Cir. 1987); with the Eighth Circuit decision that prevented state interference with the same FERC wholesale rates and sales at issue here, *Middle South Energy, Inc.* v. *Arkansas Public Service Commission*, 772 F.2d 404 (8th Cir. 1985), *cert. denied*, 106 S. Ct. 884 (1986); and with numerous state supreme court decisions. *E.g.*, *Northern States Power Co.* v. *Minnesota Public Utilities Commission*, 344 N.W.2d 374 (Minn.), *cert. denied*, 467 U.S. 1256 (1984).

Because this case is squarely controlled by *Nantahala*, summary reversal would be appropriate. In the alternative, the Court should set the case for full briefing and argument.

MP&L And The Middle South System. Mississippi Power and Light Company ("MP&L") is an electric utility that provides retail electric service to the approximately 333,000 customers in the western half of Mississippi. MP&L's electric generation and transmission facilities are planned, constructed, and operated on a coordinated basis with those of three affiliated utilities: Arkansas Power & Light Company ("AP&L"), Louisiana Power & Light Company ("LP&L"), and New Orleans Public Service Inc. ("NOPSI"). MP&L and these affiliated companies are each wholly-owned subsidiaries of Middle South Utilities, Inc. ("MSU"), and they form an integrated interstate power pool known as the Middle South System.

The Middle South System operating companies provide electricity to the public in four states—Mississippi, Arkansas, Missouri, and Louisiana—and the companies are regulated by five different state or local regulatory authorities in these states.[3] MP&L is the only Middle South operating company regulated by the Mississippi Public Service Commission ("Mississippi PSC").

Arrangements among Middle South System operating companies for the transmission, sale, and exchange of power have been governed by power pool agreements ("System Agreements") that are filed with and subject to the exclusive jurisdiction of FERC. Under the System Agreements, planning for new generating capacity is coordinated by a system-wide operating committee made up of a representative from each operating company and MSU.

In 1974, MSU formed a new subsidiary, Middle South Energy, Inc. ("MSE") (now named System Energy Resources, Inc.) to

[3]AP&L is regulated by the Arkansas Public Service Commission and the Missouri Public Service Commission; LP&L is regulated by the Louisiana Public Service Commission and, with respect to one ward of the City of New Orleans, the Council of the City of New Orleans; NOPSI is regulated by the Council of the City of New Orleans; and MP&L is regulated by the Mississippi Public Service Commission.

finance, construct, and operate a nuclear-fueled generating station near Port Gibson, Mississippi ("Grand Gulf 1"). 31 FERC at 61,653-54; App. 118a-120a. The information available at the time showed that construction and completion of Grand Gulf 1 would produce enormous savings for all of the companies of the Middle South System and should be undertaken as a System project. *Middle South Energy, Inc.*, 26 FERC (CCH) ¶ 63,044, at 65,101-02 (1984). However, subsequent regulatory delays, high inflation, and the regulatory requirements imposed after the 1979 accident at Three Mile Island caused the cost of construction of Grand Gulf 1 to increase substantially. 26 FERC at 65,103. Nonetheless, MSE completed Grand Gulf 1 because it continued to appear that the cost per kilowatt hour of energy from Grand Gulf 1 would be less than alternative gas and oil-fired generating facilities. 26 FERC at 65,112-13. Indeed, a principal reason for the construction of Grand Gulf 1 and other Middle South nuclear plants had been to diversify Middle South's fuel sources and reduce its dependence on plants that use oil and natural gas—the prices of which had dramatically escalated in the 1970s and early 1980s. 31 FERC at 61,651-53; App. 115a-118a.

The FERC Proceedings. In 1982, the Middle South companies entered into a new System Agreement to replace the earlier 1973 System Agreement. They also entered into a Unit Power Sales Agreement with MSE ("UPSA") that allocated the capacity and costs of Grand Gulf 1 among MP&L, LP&L, and NOPSI but contained a "0%" allocation to AP&L (which serves Arkansas and Missouri). These agreements were filed with FERC for its review, and the UPSA was denominated MSE's FERC Rate Schedule No. 1. FERC instituted two separate dockets to investigate the reasonableness of these two agreements.

FERC, the Middle South companies, and government officials and Middle South customers in the affected states all recognized that the FERC decision in this wholesale rate proceeding would have "substantial rate impacts" for the four Middle South oper-

ating companies and the retail customers in each of the four Middle South states. *Middle South Energy, Inc.*, 32 FERC (CCH) ¶ 61,207, at 61,478 (1985).[4] For this reason, the state public utility commissions, local regulatory agencies, and other public authorities in each jurisdiction served by the Middle South System intervened in the FERC proceedings. Each urged a different allocation and rate that would promote the interests of ratepayers in its jurisdiction. Thus, Arkansas and Missouri defended the 0% allocation made to AP&L in the UPSA. Louisiana, Mississippi, and New Orleans authorities, in contrast, vigorously challenged that allocation.

The Mississippi PSC and each of the appellees in this case (the Mississippi Attorney General and the Mississippi Legal Services Coalition) participated in the proceedings before FERC. 31 FERC at 61,629; App. 74a. They contended that MP&L had no current need for Grand Gulf 1 capacity and urged an allocation formula—based on reinstatement of the earlier 1973 System Agreement—under which Mississippi would not be allocated any of the Grand Gulf 1 costs and power until the mid-1990s. 31 FERC at 61,635-36; App. 85a-86a. Alternatively, MP&L and other Mississippi parties urged FERC to prescribe an allocation formula in which Mississippi would receive a far lower allocation (approximately 14½%) than contained in the UPSA as filed in 1982. 31 FERC at 61,638; App. 90a-91a.

[4]For example, one of the two administrative law judges that considered these matters emphasized:

> "[O]nce [FERC] allows a utility to charge a rate reflecting investment in a particular plant, the State commission with regulatory authority over the utility is required by the Supremacy Clause of the United States Constitution to allow the utility to recover the cost of the FERC approved rate in its retail rates. . . ."

Middle South Services, Inc., 30 FERC (CCH) ¶ 60,030, at 65,149 (1985) (citations omitted). FERC "explicitly adopted" this conclusion (32 FERC at 61,951-52; App. 171a), and the Court of Appeals affirmed it in its later decision that upheld FERC's order. *Mississippi Industries* v. *FERC*, 808 F.2d 1525, 1548-49 (D.C. Cir. 1987), *vacated in part on other grounds and rehearing en banc granted*, 814 F.2d 773 (D.C. Cir. April 3, 1987).

After three years of proceedings, FERC issued its final decision in FERC Opinions 234 and 234-A. App. 73a-152a, 153a-195a. FERC found that Grand Gulf 1 had been reasonably planned and built to meet the needs of the entire System[5] and that the costs of Grand Gulf 1 "should be shared equitably by all four operating companies and their customers." 31 FERC at 61,632-33; App. 80a. FERC further found that "just, reasonable and non-discriminatory rates" among the Middle South companies would not exist unless the investment in all the System's nuclear-fueled units is "equalized" so that each System operating company shares "the cost of nuclear capacity roughly in proportion to each company's share of System demand." 31 FERC at 61,656; App. 123a. Thus, FERC overrode the parties' agreement and prescribed wholesale rates and allocations of Grand Gulf 1 costs and power that dramatically changed the entitlement percentage in the UPSA:

	UPSA, as filed	Allocation under Opinion No. 234
AP&L	0%	36%
LP&L	38.57%	14%
MP&L	31.63%	33%
NOPSI	29.80%	17%

[5]In FERC rate proceedings, all costs are presumed to be prudently incurred and will be included in wholesale rates unless objections are raised to their reasonableness. *Minnesota Power & Light Co.*, 11 FERC (CCH) ¶ 61,312, at 61,645 (1980); *New England Power Co.*, 31 FERC (CCH) ¶ 61,047 (1985), *aff'd sub nom. Violet* v. *FERC*, 800 F.2d 280 (1st Cir. 1986). Nonetheless, the Middle South companies introduced uncontradicted evidence that the decisions to initiate Grand Gulf 1 and to complete construction were reasonable and prudent and that the entire Grand Gulf 1 investment should therefore be included in MSE's rate base. FERC established wholesale rates for MSE that did precisely that. *See, e.g.*, 26 FERC at 65,101-03; 31 FERC at 61,651-56; App. 118a-123a. Moreover, contrary to the Mississippi Supreme Court's statement (App. 17a), Administrative Law Judge Liebman expressly found that completion of the unit was "prudent":

> "[C]ontinuing construction of Grand Gulf Unit No. 1 *was prudent* because Middle South's executives believed Grand Gulf would enable the Middle South system to diversify its base load fuel mix

(Footnote continued on next page)

In so holding, FERC rejected the proposed lower allocations of the Mississippi parties (32 FERC at 61,958-61; App. 185a-190a) and all contentions that allocations should be based on the current "needs" of the individual operating companies, irrespective of "the greater interests of the entire System." 32 FERC at 61,958; App. 184a-185a.

The Mississippi PSC, the Mississippi Attorney General, the Mississippi Legal Services Coalition, MP&L, AP&L, various organizations representing customers, public utility regulatory authorities, and various governmental authorities from Louisiana, Arkansas, and Missouri all appealed the FERC decision to the United States Court of Appeals for the District of Columbia Circuit. On January 6, 1987, the Court of Appeals unanimously ruled that FERC has exclusive jurisdiction over the UPSA because it involved an interstate sale of power at wholesale from MSE to Middle South operating companies. *Mississippi Industries* v. *FERC*, 808 F.2d 1525, 1539-53 (D.C. Cir. 1987). The Court of Appeals also unanimously rejected the argument of the Mississippi Attorney General, the Mississippi PSC, and the Mississippi Legal Services Coalition that none of the Grand Gulf 1 power and costs should be allocated to Mississippi. *Id.* at 1564-65. Finally, the Court of Appeals also sustained, by a divided vote, FERC's specific percentage allocations of Grand Gulf 1. *Id.* at 1560-62. Judge Bork dissented only from the portion of the decision upholding the specific percentage allocations. *Id.* at 1568-69.

On April 3, 1987, the Court of Appeals *en banc* vacated that portion of the panel decision that deals with the adequacy of the Commission's rationale for the specific allocations of Grand Gulf 1

(Footnote continued from previous page)

and, it was projected, at the same time, produce power for a total cost (capacity and energy) which would be less than existing alternatives on the system."

26 FERC at 65,112-13 (emphasis supplied). This finding was not challenged before FERC or the Court of Appeals.

costs and power among the operating companies, ordered reargument *en banc* on the issues raised by Judge Bork's dissent, and left the remainder of the panel's decision undisturbed. 814 F.2d 773 (D.C. Cir. 1987).

In the meantime, the FERC-prescribed rates and percentage allocations continue in full force and effect. Neither FERC nor the Court of Appeals has stayed FERC Opinions 234 and 234-A.

The Mississippi Retail Ratemaking Proceedings. Grand Gulf 1 began commercial operations on July 1, 1985. The FERC decision required MP&L thereupon to begin paying MSE about $27 million per month ($906,000 a day) for Grand Gulf 1 power.[6] To obtain the revenues required to pay this expense, MP&L filed an application for a retail rate increase with the Mississippi PSC. The only issue in this retail rate proceeding (and in the subsequent appeal) was the proper treatment of MP&L's Grand Gulf 1 expense; all other issues were determined by stipulation.

On September 16, 1985, the Mississippi PSC issued an order that assures that MP&L would recover all of its Grand Gulf 1 expenses, but that "phases-in" the increase to moderate its impact on retail customers.[7] The MP&L retail rate schedule and Missis-

[6]MP&L's monthly bills for Grand Gulf 1 power have since declined to about $25 million a month (or about $820,000 per day), primarily due to depreciation.

[7]The order phases-in the retail rate increase necessary to recover MP&L's Grand Gulf 1 expenses over a 10-year period and requires MP&L to spread the actual recovery of its Grand Gulf costs over a 40-year period. Thus, MP&L was initially permitted to collect from its customers only about $8 million of its monthly Grand Gulf 1 costs, with that amount increased to $12 million on October 1, 1986. Under the Mississippi PSC order, MP&L must defer the balance and carry the deferred amount on its books as a deferred asset. Thus, the order has placed an extraordinary burden on MP&L to finance more than half of its Grand Gulf 1 costs. To date, MP&L has been able to borrow sufficient funds to meet its expenses because the order provides assurance that all of MP&L's Grand Gulf 1 costs will ultimately be recovered.

sippi PSC order further provide that Mississippi retail rates will be immediately reduced and any other savings "flowed through" to retail customers to the extent that FERC hereafter modifies the Grand Gulf 1 wholesale rates and allocations to reduce MP&L's share. *See* App. 51a.

The Mississippi Attorney General and the Mississippi Legal Services Coalition appealed the Mississippi PSC order to the Mississippi Supreme Court. They there made the precise arguments that FERC had rejected in its decisions: that Mississippi would not "need" any Grand Gulf 1 electricity until at least the mid-1990s; that the 1973 agreement would produce a fairer allocation; that no Grand Gulf 1 costs should be imposed on Mississippi ratepayers at this time; and that, in any event, FERC's 33% allocation to MP&L was excessive. *See* App. 2a-3a. MP&L responded that FERC's determination of "just and reasonable" rates was binding on the Mississippi PSC and that the PSC had no jurisdiction to investigate, alter, or disregard the wholesale cost allocations established by FERC in setting wholesale rates.

On February 25, 1987, the Mississippi Supreme Court reversed the Mississippi PSC's order, over Justice Robertson's dissent. The Court recognized that FERC's orders and rate schedules required MP&L to pay $906,000 per day for Grand Gulf 1 power. App. 11a. However, the Mississippi Supreme Court held that under *Miss. Code Ann.* § 77-3-39 (Supp. 1986), the Mississippi PSC is required to make its own determination of the "prudence" of MP&L's Grand Gulf 1 costs on the basis of local needs and conditions *before* any of those costs could be recovered from Mississippi ratepayers. App. 13a-20a.

In doing so, the Mississippi Supreme Court refused to give any effect at all to FERC's allocations of the costs and power of Grand Gulf 1. The Mississippi Supreme Court stated that FERC's allocation of 33% of Grand Gulf 1 costs to MP&L was clearly "excessive" and "imprudent" (App. 16a):

> "In light of these facts, clearly the allocation of 33% of Grand Gulf power is unreasonably excessive. Since Mississippi cannot use 33% of Grand Gulf's power, the 1982 System Agreement providing for the allocation of 33% of its cost would seem to be imprudent."

It further found that there is "no doubt that Mississippians do *not* need the power provided by Grand Gulf" (App. 15a) (emphasis in original) and that Mississippi ratepayers are being burdened with energy costs they cannot afford because of costs allocated by FERC to MP&L (App. 16a):

> "[W]e believe that . . . Mississippi ratepayers are being intolerably burdened with high-cost nuclear energy that they neither want nor need nor can afford."

And it concluded that the FERC had no right to force "unneeded power down the throats of Mississippi ratepayers" (App. 15a). In the Mississippi Supreme Court's view, the entire question was a local one, appropriate for review only by the Mississippi PSC using its expertise in local conditions (App. 18a-19a):

> "In remanding this case to the MPSC for a review of the prudency of the Grand Gulf investment, we rely on the expertise of this agency in making a determination of whether MSU and its subsidiaries made reasonable decisions *in light of local conditions*." (Emphasis in original.)

The Court held that until the Mississippi PSC made this prudence review based on local conditions, MP&L could not be granted any rate increase based on Grand Gulf 1 costs (App. 19a):

> "We thus hold that the state regulatory body, in this case, the Mississippi Public Service Commission, must review the prudency of an investment such as Grand Gulf *before* it can enact rates based on its cost." (Emphasis supplied.)

The Mississippi Supreme Court denied MP&L's timely petition for rehearing on May 20, 1987. App. 197a-198a. On May 26, 1987, the Mississippi PSC thereupon took the action required by

the Mississippi Supreme Court's mandate. It entered an order rescinding the September 16, 1985 rate increase and ordered MP&L to submit a plan for refunding the entire Grand Gulf 1 expense that had been recovered from retail ratepayers under the Mississippi PSC's earlier order. App. 199a-200a.

On June 1, 1987, this Court stayed the judgment of the Supreme Court of Mississippi "pending the timely filing and disposition of [this] appeal by this Court."

THE QUESTION PRESENTED IS SUBSTANTIAL

The question presented in this case is not only substantial; it is indistinguishable from the issue decided last term in *Nantahala Power & Light Co.* v. *Thornburg,* No. 85-568, 106 S. Ct. 2349 (June 17, 1986). Both cases involve a single common factual pattern. In both, FERC exercised its exclusive jurisdiction under the Federal Power Act to set "just and reasonable" wholesale rates that allocated wholesale power costs among commonly-owned companies that serve different states. In both cases, an affected state participated in FERC proceedings and unsuccessfully urged allocations that were more favorable to its citizens. And in both cases, this affected state then attempted to use its retail rate proceedings to nullify FERC's determination and to re-allocate the same costs to that state's own benefit and to the detriment of its neighbor. This conduct violates the Federal Power Act and the Commerce Clause.

Federal Power Act Preemption. Justice Robertson's dissent is correct. The Mississippi Supreme Court has entered "an area" that, under *Nantahala,* is "wholly preempted by authority granted by the Congress to the Federal Energy Regulatory Commission." App. 23a. *Nantahala* holds that, under the "filed rate doctrine," wholesale rates "filed with FERC or fixed by FERC must be given binding effect by state utility commissions determining intrastate rates." Slip op. at 8; 106 S. Ct. at 2354. And

Nantahala unequivocally condemned the kind of state interference with the implementation of federal decisions that Mississippi has ordered (slip op. at 13; 106 S. Ct. at 2357):

> "FERC clearly has exclusive jurisdiction over the rates to be charged Nantahala's interstate wholesale customers. . . . Once FERC sets such a rate, a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A state must rather give effect to Congress's desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority."

The holding of *Nantahala* governs this case. FERC determined the "just and reasonable" rates for Grand Gulf 1 power in proceedings that spanned three years. Representatives of every affected jurisdiction fully participated, and the Mississippi PSC, Mississippi Attorney General, and the Mississippi Legal Services Coalition urged allocations in which MP&L would incur no Grand Gulf 1 costs until it "needs" that power in the mid-1990s or, alternatively, 14½% of the Grand Gulf 1 investment. FERC, however, rejected Mississippi's arguments on the basis of its assessment of the Middle South interstate system as a whole and allocated 33% of the Grand Gulf 1 power and costs to MP&L and its customers.

Under *Nantahala,* the Mississippi PSC must treat those FERC-allocated costs "as a reasonably incurred operating expense for the purposes of setting an appropriate retail rate" unless and until FERC again alters the "filed rate." Slip op. at 13; 106 S. Ct. at 2357 (citation omitted). Otherwise, the Mississippi PSC could prohibit MP&L's recovery of $820,000 per day that the FERC orders require MP&L to pay MSE, and MP&L would be left with "trapped costs" of some $25 million each month. *See* slip op. at 17-18; 106 S. Ct. at 2359.

The Mississippi Supreme Court attempts to distinguish *Nantahala* by contending that it does not require a state commission

to recognize FERC-approved wholesale rates for "power that is not needed at a price that is not prudent." App. 15a. This is simply a direct attack on *Nantahala's* core holding. What the Mississippi Supreme Court is saying is that the Mississippi PSC could find that Mississippi does not "need" Grand Gulf 1 power because its costs are too high and Mississippi should have been allocated other, "lower cost power [that] is available elsewhere" in the Middle South System. App. 15a. FERC rejected this very argument. In its proceeding, FERC had *all* the power sources from the Middle South System before it, and FERC decided that an allocation of 33 percent of the higher-cost Grand Gulf 1 power to MP&L is "just and reasonable."

In this respect, as in all others, the case is identical to *Nantahala.* The North Carolina Supreme Court's position in *Nantahala* was that the North Carolina utility (Nantahala Power & Light Co.) did not "need" any of the more expensive purchased power because it could take more of the less expensive entitlement power. The Court rejected that argument because in *Nantahala,* as here, FERC's rate schedules and decisions allocated the higher-cost power and did *not* give the local utility access to more of the low-cost power. Slip op. at 19; 106 S. Ct. at 2360.

For these reasons, the Mississippi Supreme Court is in error in suggesting (App. 15a) that this case presents the question, reserved in *Nantahala,* of whether a utility's "purchase" of a "particular *quantity* of power . . . from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere . . . ." Slip op. at 19; 106 S. Ct. at 2360 (emphasis in original). The dispositive fact here, as in *Nantahala,* is that FERC, not the purchasing utility, made the determination of how much Grand Gulf 1 power MP&L would pay for and how applicable power supplies and costs would be allocated within a single integrated multi-state system.[8] Here, as in *Nantahala,*

[8]Indeed, FERC allocated 36% of the Grand Gulf 1 power and costs to AP&L when it had not agreed to pay for *any* of that power.

MP&L "could not have treated itself" as subject to an allocation of power supplies and costs that is different from "FERC's interpretation of what would be a fair allocation." Slip op. at 19; 106 S. Ct. at 2360.

Whether the issue is North Carolina versus Tennessee, or Mississippi versus Arkansas, Louisiana, and Missouri, the principle is the same. FERC, a neutral forum, must have exclusive jurisdiction to set just and reasonable wholesale rates and to allocate power costs among interested states. Otherwise, each state will seek to impose allocations that advance its interests at the expense of its neighbors.

The Mississippi Supreme Court similarly asserts that federal preemption extends only to "matters *actually determined,* whether expressly or impliedly, by the FERC." App. 17a, *citing Appeal of Sinclair Machine Products, Inc.,* 126 N.H. 822, 833, 498 A.2d 696, 704 (1985) (emphasis in original). The Mississippi court contends, in this regard, that there are "several aspects" of MP&L's "prudency" that were not at issue in the FERC proceedings and that state authorities can now make these determinations. However, each issue that the Mississippi Supreme Court raises was included in FERC's determination of the "just and reasonable" rates under which MP&L and other Middle South companies are to acquire power "for resale" to retail customers. FERC found that it was "just and reasonable" to include 100% of the Grand Gulf 1 investment in MSE's rate base and then to allocate all the Grand Gulf 1 capacity and costs among the Middle South operating companies. FERC thus determined that initiation and completion of the plant at its cost was "just and reasonable" for the Middle South System *as a whole. See* pp. 7-8 & n.5, *supra.*[9]

[9]As the Fourth Circuit has held, a FERC finding that a wholesale cost allocation and rates is "just and reasonable" is a determination of "prudence." *Appalachian Power Co.* v. *Public Service Commission of West Virginia,* 812 F.2d 898, 903-04 (4th Cir. 1987).

The Mississippi Supreme Court further contends that the question of the reasonableness of the Grand Gulf 1 investment should be treated as a local issue whose "prudence" must be independently assessed by the Mississippi PSC "*in light of local conditions*" and the "needs" of individual companies. App. 18a-19a (emphasis in original). This, too, is a challenge to FERC's explicit holding (32 FERC at 61,958; App. 184a-185a):

> "The argument that allocation of Grand Gulf costs should be based on whether individual companies 'need' Grand Gulf capacity must be rejected. . . . The record evidence relied upon in Opinion No. 234 establishes that Grand Gulf was built primarily to serve the System as a whole and to meet the System goal of obtaining a greater proportion of nuclear capacity. Our task, therefore, is one of allocating costs consistent with the mandate of the Federal Power Act, and the allocation of Grand Gulf power must rest not on the 'needs' of an individual company, but rather on the principles of just, reasonable, non-discriminatory, and non-preferential rates."

As the Court has held, "the production and transmission" of electrical energy is "particularly likely to affect more than one State," and "broader national interests" require that this activity be regulated by a federal agency that will assess regional and national needs, not purely local ones. *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Commission*, 461 U.S. 375, 377 (1983); *see FPC* v. *Southern California Edison Co.*, 376 U.S. 205 (1964).

These principles have also been recognized by state supreme courts. Indeed, the Mississippi Supreme Court's holding that states may disallow FERC-approved costs on the basis of the states' own findings that power is not "needed" at a particular price squarely conflicts with *Northern States Power Co.* v. *Minnesota Public Utilities Commission*, 344 N.W.2d 374 (Minn.), *cert. denied*, 467 U.S. 1256 (1984); *Northern States Power Co.* v. *Hagen*, 314 N.W.2d 32 (N.D. 1981); and *Narragansett Electric*

Co. v. *Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), *cert. denied*, 435 U.S. 972 (1978).[9]

Finally, it is irrelevant that appellate review of FERC Opinions 234 and 234-A is still pending and that FERC may conceivably hereafter revise the Grand Gulf 1 allocations—due to the forthcoming *en banc* decision of the Court of Appeals or otherwise. *See* pp. 8-9, *supra*. The FERC Grand Gulf 1 allocations have not been stayed by FERC, or by the Court of Appeals. Unless and until it is changed, the FERC decisions thus establish a "filed rate" that must be respected under *Nantahala*. A state commission's sole means of protecting the interests of retail ratepayers is to do what the Mississippi PSC did here: participate in the federal proceedings and make provisions in its retail rate order for reductions or refunds to the extent FERC later reduces MP&L's allocations and obligations. *See* pp. 9-10, *supra; Narragansett Electric Co.* v. *Burke*, *supra*, 119 R.I. at 568, 381 A.2d at 1363.

Commerce Clause Violation. The Mississippi Supreme Court's decision also violates the Commerce Clause. That Clause flatly prohibits a state's attempts to reserve the benefits of low-cost electric energy for its citizens, contrary to FERC's regulation. *New England Power Co.* v. *New Hampshire*, 455 U.S. 331 (1982). It is equally clear that a state may not embargo high-cost power.

Indeed, the Mississippi Supreme Court's decision on this issue is in direct conflict with the Eighth Circuit decision that prevented state interference with the same FERC rate schedules at issue

[9]The *Northern States* decisions are especially pertinent because each involves a nuclear plant that had been abandoned and that, with the benefit of hindsight, had not been "needed." Each state supreme court nonetheless held that the costs allocated to its state by FERC had to be treated as "reasonable operating expenses" and recovered in retail rates. In contrast to the Mississippi Supreme Court, the *Northern States* courts hold that "the reasonableness and prudence" of these investments are exclusively matters for determination by FERC. *Northern States Power Co.* v. *Hagen*, 314 N.W.2d at 38; *see Northern States Power Co.* v. *Minnesota Public Utilities Commission*, 344 N.W.2d at 377-81.

here under these Commerce Clause principles. *Middle South Energy, Inc.* v. *Arkansas Public Service Commission*, 772 F.2d 404 (8th Cir. 1985), *cert. denied*, 106 S. Ct. 884 (1986). In *Middle South Energy*, the Arkansas Public Service Commission instituted an investigation that was designed to prevent Arkansas ratepayers from incurring the Grand Gulf 1 costs assigned them by FERC Opinions 234 and 234-A. The Eighth Circuit enjoined the Arkansas PSC's proceedings on the ground that they represented a patent violation of the Commerce Clause. 772 F.2d at 416-17. There is no distinction between the actions of Mississippi and Arkansas.

CONCLUSION

The Court should note probable jurisdiction. Because this case is so squarely governed by *Nantahala*, summary reversal would be appropriate. Alternatively, the Court should set the case for argument as promptly as its schedule permits.

Respectfully submitted,

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi 39205
(601) 354-2385

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 331-9400

Of Counsel:
WISE CARTER CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN, SUTCLIFFE & CURTIS

Attorneys for Appellant

June 8, 1987

**Counsel of Record*

APPENDIX

86 1970

(2)

No. 86-

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court
of Mississippi

APPENDIX TO JURISDICTIONAL STATEMENT

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi
39205
(601) 354-2385

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 331-9400

Attorneys for Appellant

Of Counsel:
WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

Counsel of Record

205 pp

TABLE OF CONTENTS

APPENDIX A

Opinion Of The Mississippi Supreme Court

IN THE SUPREME COURT OF MISSISSIPPI
NO. 56,762

STATE OF MISSISSIPPI, EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL, ET AL.

V.

MISSISSIPPI PUBLIC SERVICE COMMISSION, ET AL.

[Decided February 25, 1987]

EN BANC

DAN LEE, JUSTICE, FOR THE COURT:

This is an appeal from an order issued by the Mississippi Public Service Commission (MPSC) on September 16, 1985, in which Mississippi Power & Light Company (MP&L) was granted the largest rate increase it has ever requested, based on the costs associated with the Grand Gulf I Nuclear Power Plant (Grand Gulf). In granting the increase, on September 16, 1985, the MPSC found that MP&L had a revenue deficiency of and granted an additional increase of $326,547,000.00, despite the fact that it had granted MP&L an increase of $44,671,544.00 in June, 1985. Collection of the $326,587,000.00 increase was ordered over a ten year period.

The Mississippi Attorney General and the Mississippi Legal Services Coalition (MLSC) have appealed, assigning as error:

1) The adoption of retail rates to pay Grand Gulf expenses without first determining that the expenses were prudently incurred;

2) Substantive *ex parte* communications between the MPSC and other parties to this cause;

3) The *ultra vires* act of the MPSC in adopting prospective rates to go into effect in the future without regard to whether they will then be just, reasonable, and nondiscriminatory;

4) The failure to join Middle South Utilities and Middle South Energy, Inc. as parties to this cause;

5) The adoption of rates without substantial evidence to support the utilization of a projected test year;

6) MP&L's estoppel from seeking reimbursement of expenses greater than that originally represented to the MPSC when the Certificate of Need was issued;

7) Intervention of resident security holders;

8) Failure of the MPSC to follow procedural orders in conducting the rate hearing;

9) Adopting rates without substantial evidence of need; and

10) Allowing rates to reflect Grand Gulf costs that are not just and reasonable.

We find that Assignments 1, 4 and 7 have merit. Because MP&L and its sister and parent companies have used the jurisdictional relationship between state and federal regulatory agencies to completely evade a prudency review of Grand Gulf costs by either agency, we reverse and remand this case to the MPSC for futher proceedings.

THE FACTS

Middle South Utilities, Inc. (MSU) consists of four operating companies (companies that actually generate electricity) and two service companies. The operating companies are: Arkansas Power & Light Company (AP&L), Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (MP&L), and New Orleans Public Service, Inc. (NOPSI). The service companies are: Middle South Services, Inc. (MSS), which provides technical and professional services to the operating companies, and Middle South Energy, Inc. (MSEI), formed in 1973 to finance the Grand Gulf project. In July, 1986, after the hearings before the MPSC in this case, MSEI changed its name to System Energy Resources, Inc. (SERI).

The operating companies all issue common, (the only voting) stock, preferred (non voting) stock, and bonds. *All* of the common stock of each operating company, however, is held by MSU. The Chief Executive Officer of MSU, by voting the common stock of each operating company, is solely empowered to elect all of the directors for each operating company, and these directors then elect the officers of their companies. One important function of the Chief Executive Officers of the operating companies is to sit on the Operating Committee, which makes major system-wide decisions. Thus, the Operating Committee's decisions are made by officers all of whom are *completely* under the control of the Chief Executive Officer of MSU.

The MSU subsidiaries operate as an integrated system. Although the companies generally own their own power plants, they pool their generated electricity. This electricity is coordinated among the operating companies in response to their needs. A dispatching facility in Pine Bluff, Arkansas, allocates the energy produced by all of the companies, with each company meeting its needs first with the lowest cost energy that it can produce. If a company needs more energy than it can produce, it is allocated higher cost energy from the other operating companies. When the entire system produces more energy than it can use, the excess energy may be sold off the system.

In addition to sharing energy, the operating companies also share in the cost of energy-producing capacity. The method of allocating the cost of capacity has changed, by agreement of the operating companies, since the construction of Grand Gulf was authorized by the MPSC in 1974, and this change is one of the primary issues of this litigation.

In 1973, MSU and its subsidiaries reached an agreement which equalized the ownership costs of generating capacity throughout the MSU system. In that agreement, companies owning capacity in excess of that required to meet their needs were referred to as "long" companies. Companies requiring additional capacity to meet their needs were referred to as "short" companies. Under the concept of equalization, short companies had to share in the costs of the generating units owned by the long companies. The short companies' allocation was calculated on the basis of the costs of the long companies' most recently installed generating units, called "participation units."

When the 1973 System Agreement became effective, MSU was planning the Grand Gulf Nuclear Station. The original plan was to build one nuclear plant at the Grand Gulf site, under the management and control of MP&L, and one plant in Louisiana, under the control of NOPSI. However, the NOPSI site proved unsuitable, and MP&L, alone, could not finance a nuclear generating plant; therefore, MSEI (now SERI) was formed to provide financing for two nuclear generating plants at Grand Gulf.

In 1974, the MPSC issued its "Order Granting Certificate of Public Convenience and Necessity" authorizing the construction of Grand Gulf. MSEI, the actual owner of the proposed two-unit facility, joined MP&L as a petitioner. The Order reflected the understanding of all of the parties involved that the 1973 Agreement would be amended to include MSEI as a party.

We cannot stress enough the implications of this agreement embodied in the 1974 Order. MSEI is not an operating company; therefore, it does not require any generating capacity for itself. Under the 1973 Agreement, it would always be a long company, with excess capacity to allocate among the short companies. Grand Gulf, its most recently installed generating unit, would become MSEI's participation unit, from which the costs to the short companies would be calculated.

At the time that the Certificate of Need was granted, it was projected that Mississippi's demand for power would increase to the point where MP&L would utilize about 38% of Grand Gulf. That demand has not materialized, and MP&L remains a long

company. Under the 1973 Agreement, it would not be required to share in the allocation of costs of Grand Gulf unless and until it required additional capacity to meet its needs. Even if the increased consumption had materialized however, and MP&L had become a short company, it would have had to pay costs associated with Grand Gulf only to the extent that it required additional capacity.

In the later 1970's, MSU management began to have concern about the 1973 Agreement. Since the demand forecasts showed that MP&L and AP&L were long companies, and would remain so for some time, they would not need to purchase capacity until the planned nuclear plants had been greatly depreciated. Thus, they would not be required to bear the brunt of the costs of nuclear construction, as would the short companies. MSU's Operating Committee, consisting of the Chief Executive Officers of AP&L, LP&L, MP&L and NOPSI, studied the situation for several years, and, in the 1980, voted to adopt a new system agreement.

The new agreement, referred to throughout these proceedings as the 1982 System Agreement, eliminated the participation unit concept. Instead, the companies were to implement the use of "intermediate Generating Units," defined as oil and gas burning units, to allocate the cost of capacity. The rationale for the change was as follows: Nuclear units, with their high fixed costs and low fuel costs, are run around the clock to provide the operating companies with base capacity. Oil and gas units, with their low fixed costs and high fuel costs, are primarily operated to provide reserve capacity: for instance, on hot summer days. Thus, excess capacity is more likely to have come from the operation of oil and gas burning, rather than nuclear, generating units. The effect of this change was that capacity allocated to companies in the MSU system was calculated on the cost of the generating oil and gas units, at a fraction of the cost of nuclear energy.

MSEI had no oil and gas burning units and was not a party to the 1982 System Agreement. It required however, a methodology

for the allocation of the cost of the nuclear capacity at Grand Gulf. To that end, MSEI entered into a Unit Power Sales Agreement (UPSA) with the operating companies. The UPSA allocated Grand Gulf 1 among the operating companies as follows:

LP&L	38.57%
MP&L	31.63%
NOPSI	29.80%
AP&L	0.00%

The UPSA was not filed with MPSC. However, it was filed with the Federal Energy Regulatory Commission (FERC) in Docket No. ER82-616-000. The 1982 System Agreement was filed with the FERC in Docket No. ER82-483-000.

At about the same time that they agreed on the UPSA, the MSU operating companies and MSEI entered into a Power Purchase Advance Payment Agreement. This agreement provided that the companies would pay MSEI in advance for Grand Gulf power. The payments, which totalled $12,500,000.00 per month for all of the companies, were to be made from January, 1984, through December, 1985, or whenever Grand Gulf became operational. Eighteen payments were made under this agreement; MP&L paid 33% of the total. The agreement provided that on the date that Grand Gulf became operational, and for eleven months thereafter, the companies would be reimbursed for 4% of the outstanding balance of the advances. The companies would get 8⅓% for the next six months, and then the balance. MP&L's share of the agreement may be calculated as follows:

$12,500,000.00/month X 18 months = $225,000,000.00 (the total amount of payments)

$225,000,000.00 X 33% = $74,250,000.00 (MP&L's share of the total payments)

$74,250,000.00 X 4% = $2,970,000.00 (first reimbursement to MP&L)

The last figure would be adjusted upward to interest accrued on the funds advanced to MSEI. The actual rebate to MP&L on its first Grand Gulf bill was $3,232,727.41.

In 1984, FERC Administrative Law Judge Liebman issued his opinion in ER82-616-000, which dealt with the UPSA filing. He found the Grand Gulf allocation under the UPSA to be unjust and unreasonable, as was the proposal made by the MPSC to return to the 1973 Agreement and make Grand Gulf a participation unit. In order to allocate the costs of nuclear power throughout the MSU system, he ordered the following allocation for Grand Gulf 1:

LP&L	14%
MP&L	33%
NOPSI	17%
AP&L	36%

On February 4, 1985, FERC ALJ Head issued his order in ER82-483-000, which dealt with the 1982 System Agreement filing. He ruled that Grand Gulf was an anomaly in the MSU system that should be allocated among the operating companies, with the allocation fluctuating from year to year, based on each company's demand for system energy. The effect of that decision would be to allocate approximately 14½% of Grand Gulf to MP&L.

In November, 1984, when the operational status of Grand Gulf became imminent, MP&L filed for the rate increase which is the subject of this case. In addition to the Grand Gulf expense, MP&L sought a rate increase for the purchase of part of the Independent Steam Electric Station Unit 2 (ISES2), a coal-burning plant located in Arkansas. MP&L bought 25% of the ownership, and 31.5% of the capacity of the plant, which was owned by a sister company, AP&L. It is agreed by all of the parties to this appeal that this purchase will result in lower fuel costs, which will be passed on to consumers through the fuel adjustment clauses in

their bills. A rate hearing was held on January 15, 1985, for interim rates for the ISES2 purchase, and, on January 17, the MPSC issued an interim order granting approximately $45 million in increased revenues associated with ISES2. This order is not at issue in this appeal, except to the extent that it adds to the excess capacity imposed upon MP&L by the Grand Gulf allocation.

The primary objection to the allocation of Grand Gulf to MP&L is that Mississippi ratepayers simply do not need the energy generated by the plant. In fact, we cannot utilize this excess capacity until the mid-1990's, if ever. Frank Gallagaher, an MP&L witness, testified that with the addition of ISES2 but *before the Grand Gulf allocation*, MP&L had a reserve capacity of *85% over peak demand*. Both Gallagher and Lewis Perl, another MP&L witness, testified that the appropriate reserve margin was 30-35%. MP&L represented to the MPSC that the reserve capacity figures are unimportant, because the ratepayers only support the capacity that MP&L cannot sell off the system. Nevertheless, should MP&L be unable to peddle its excess energy to other companies, (which is the case now) Mississippi ratepayers would have to support over 100% more capacity than they can use.

On March 5, 1985, the MPSC issued an order severing the issue of prudency from the rate increase "to be heard at a later date." On April 30, the MPSC, the Attorney General, the MLSC and MP&L entered into a stipulation regarding the revenue requirements associated with the requested rate increase as to issues only. This stipulation specifically excluded the issues of prudency and excess capacity, because it had been severed by commission order on March 3, 1985.

The MPSC held another hearing on May 21, 1985. At that time, Grand Gulf 1 was expected to (and ultimately did) come on line July 1, 1985, at a kilowatt hour cost roughly equivalent to $72-85/barrel for oil. The company testified that the first bill

from MSEI for Grand Gulf was expected on August 5, 1985, and, without a rate increase, MP&L could only afford to make the payment to MSEI through November. After that, MP&L would have to curtail activities or attempt to raise the money through an equity offering. The issue of bankruptcy was discussed, and later rejected, as an alternative.

MP&L proposed a plan where revenues for the Grand Gulf expense would be recovered over a ten-year period. This plan was drawn in accordance with the UPSA allocation of Grand Gulf of 31.63%, although MP&L testified that its litigation position before the FERC was aligned with Judge Head's allocation of 14¼%. The "rate moderation plan" would allow MP&L to bill its customers at less than the Grand Gulf cost for its first five operational years, and recover the difference in the next five years. The theory behind the plan was to allow MP&L to defer part of the cost of Grand Gulf that would normally have to be recognized on its financial statements as expense. This deferral would allow the statements to reflect acceptable earning levels, so that the company could issue stocks and bonds to finance the difference. The rate moderation plan was drawn in accordance with MP&L's understanding of the requirements of Financial Accounting Standards Board (FASB) Statement No. 71, pertaining to the deferral of utility costs. (We note, in passing, that the ten-year plan is derived from a proposed amendment to FASB No. 71, and some accounting professionals have taken the position that such deferrals should be spread over the life of the plant. In this case, the revenues could be collected over the life of Grand Gulf, which is estimated to be forty years.) The plan proposed by MP&L also included provisions for low use customers and senior citizens, and provided for an annual "true up" of expenses.

On June 13, 1985, the FERC issued Opinion 234, affirming Judge Liebman's Grand Gulf allocation of 33% to MP&L, and rejecting Judge Head's allocation of 14½%. This opinion was eventually affirmed by a 2-1 vote of the Court of Appeals for the District of Columbia Circuit. *Mississippi Industries v. Federal Energy Regulatory Commission,* No. 85-1611, decided Jan. 6, 1987, not yet reported. Justice Bork dissented from the majority opinion, and would have held that FERC's allocation did not appear to remedy the alleged undue discrimination among the generating costs of nuclear energy of the operating companies.

On June 14, 1985, the MPSC granted a rate increase to MP&L for the ISES2 costs of $44,671,544.00. However, in allowing the increase, the Commission stated:

> The matter of excess capacity on the Company's system and the Middle South System as a whole continues to be of great concern to this Commission. While the interim rate relief granted in this order attributable to additional capacity is represented by Independence Unit 2, *this Commission expressly reserves all its rights to examine and investigate indepth [sic] the excess reserve or excess capacity issue* in further proceedings in this cause, and take such action in granting permanent relief as may be appropriate. [emphasis added]

On the issue of Grand Gulf relief, however, the Commission held that MP&L had failed to meet its burden of proof. Specifically, the MPSC found that MP&L's change in allocating Grand Gulf expense precluded it from seeking the increased rates. The Commission stated that, as the state regulatory agency, it should be entitled to rely on the company's prior representations. Thus, the requested rate increase for Grand Gulf was denied.

After this order was issued, the parties engaged in settlement negotiations. Presented in these discussions was a proposal that MP&L currently recognize 22% of its 33% Grand Gulf allocation, while deferring the remaining 11%. No agreement could be reached. Eventually, the MPSC granted a rehearing on the Grand Gulf rate relief which it had denied on June 14, 1985.

On July 1, 1985, Grand Gulf Unit 1 came on line, causing MP&L to begin incurring unrecovered costs of about $906,000.00 per day. On July 26, MP&L applied for temporary emergency rates, claiming that the Grand Gulf bill would cause

its net income to become negative in September. The first bill for Grand Gulf, of approximately $27 million, was sent to MP&L on August 7.

The MPSC held a hearing on the temporary rate increase on August 12, 1985. Company witnesses testified that MP&L's deteriorating financial position had caused its bond ratings to be lowered below investment grade. However, the company had not, at that time, cancelled any preferred dividends.

On August 22, 1985, pursuant to an agreement between the MPSC and the federal court, the matter was set for a rehearing. By that time, MP&L's cash situation had declined precipitously, due to the unexpected cancellation of lines of credit with local banks. At the rehearing on September 9, the company testified that it had no external sources of financing.

The MPSC issued its Final Order on Sepember 16, 1985, granting the $326 million rate increase. The order provided for recovery of Grand Gulf costs in a plan similar to the rate moderation plan originally proposed by MP&L. For the first 10 years of the plan, MP&L would inventory ⅓ of its 33% Grand Gulf allocation, with recovery of the deferred amount beginning in 1995. Of the 22% then allowed, 7.5% would be inventoried for the first three years. The net effect of the plan is illustrated by the following table:

Year	FERC Allocation		10-Year Inventory		Current Recovery		3-Year Inventory		Net Current Recovery
1	33%	–	11%	=	22%	–	7.5%	=	14.5%
2	33	–	11	=	22	–	7.5	=	14.5
3	33	–	11	=	22	–	7.5	=	14.5
4	33	–	11	=	22				22.0
5	33	–	11	=	22		recovery		22.0+
6	33	–	11	=	22		of		22.0+
7	33	–	11	=	22		7.5%		22.0+
8	33	–	11	=	22		over		22.0+
9	33	–	11	=	22		years		22.0+
10	33	–	11	=	22		5–10		22.0+

11 Recovery of 11% over life of plant.

The amount allowed as "Net Current Recovery" would be further reduced in the first three years pursuant to a phase-in schedule. The order also provided that MP&L could recover currently the incremental cost (e.g., interest on bonds) of financing the deferred inventory amounts. The ultimate cost to the consumer is as follows:

Year	Annual Increase Ordered	Cumulative Increase Over 1984 Rates
1985–86	14.07%	14.07%
1986–87	8–10%	22–24%
1987–88	8–10%	30–34%
1988–89	7–8%	37–42%
1989–90	7–8%	44–50%

I. PRUDENCY

Miss. Code Ann. § 77-3-39 (1972) authorizes the MPSC to establish just and reasonable rates which lead to a fair rate of return for the utility. As we have often held, "A fair rate is one which, *under prudent and economical management*, is just and reasonable to both the public and the utility." *Miss. Public Service Commission v. Miss. Power Co.*, 429 So.2d 883 (Miss. 1983), (citing *Southern Bell Tel. & Tel. Co. v. Mississippi Public Service Comm'n*, 237 Miss. 157, 241, 113 So.2d 622, 656 (1959) [emphasis added].

What appears to have taken place here is the evasion by sister MSU companies of any review of the prudency of their operation or the fairness of their many "in house" dealings. The C.O.N. to construct Grand Gulf was granted under a specific set of circumstances: the first unit was to be operational in 1980, the two units were to cost $1.227 billion, and Mississippi ratepayers were not to pay for any more of its capacity than they needed. Unit 1 began operation in July, 1985; the cost of Unit 1, alone, was over $3.5 billion; and the MSU-controlled operating companies agreed, *among themselves* that Mississippians should pay for ⅓ of its cost—much of Grand Gulf was even paid for in advance of receiv-

ing one kilowatt of power from the plant. Now MP&L presents us with this rate increase as a fait accompli, and demands that we affirm it, because the FERC has determined that a 33% allocation of Grand Gulf to MP&L does not discriminate among the various sister operating companies. We do not interpret the law to require that we approve the blind pass-through of a $326 million rate increase to Mississippians without a prudency review; to do so would be a gross abdication of the responsibility of state regulators.

Predictably, MP&L relies heavily on the decision of the United States Supreme Court in *Nantahala Power & Light Co. v. Thornburg*, __ U.S. __, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986). In that case, the FERC had allocated a certain amount of low cost TVA-supplied hydroelectric power to Nantahala Power & Light Company. The FERC allocation slightly adjusted an agreement between Nantahala and Tapoco, Inc., both wholly owned subsidiaries of Alcoa. Nantahala's retail customers were all North Carolina residents, and the North Carolina Utilities Commission (NCUC) rejected this allocation in its setting or rates for Nantahala. The NCUC set rates as if Nantahala were receiving more of the low cost power than it was allocated. Although the FERC allocation was ultimately approved by the United States Court of Appeals for the Fourth Circuit, the North Carolina Supreme Court affirmed the utility commission's action. The United States Supreme Court reversed.

The Supreme Court's opinion reiterated the exclusive jurisdiction of the FERC to set interstate wholesale rates. Since the allocation of low cost power directly affected Nantahala's rates, the Court held that "The fact that NCUC is setting retail rates does not give it license to ignore the limitations that FERC has placed upon Nanatahala's [sic] *available sources* of low-cost power." __ U.S. at __, 106 S.Ct. at 2358, 90 L.Ed.2d at 956.

We are aware of the effect that wholesale rates have on retail rates, and we do do not challenge the FERC's jurisdiction over in-

terstate wholesale rates. We do not, however, construe *Nantahala* as forcing the MPSC to set rates based on the construction and operation of a plant (nuclear or otherwise) that generates power that is not needed at a price that is not prudent. If MP&L had built Grand Gulf on its own, and then come to the MPSC asking for a rate increase based on its cost, no one would seriously argue that the commission would have the authority, indeed, the duty, to inquire into the prudency of its cost. MP&L, however, asks us to take the position that, because Grand Gulf is owned by an out-of-state corporation, the Supremacy clause of the United States Constitution precludes any such review of Grand Gulf, and forces its unneeded power down the throats of Mississippi ratepayers. We do not believe the preemption doctrine was ever intended to accomplish such an inequitable and unjust result.

Important factual distinctions exist between this case and *Nantahala*. In *Natahala*, no question was raised about the prudency or necessity of acquiring low-cost hydroelectric power. The Supreme Court recognized this, stating:

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive *if lower-cost power is available elsewhere*, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*.

__ U.S. at __, 106 S.Ct. at 2360, 90 L.Ed.2d at 958.

In this case, there is no doubt that Mississippians do *not* need the power provided by Grand Gulf, and that lower cost power is available elsewhere (in fact, by plants owned by MP&L). The record indicates that MP&L still serves 61% of its electrical generating needs from oil and gas units, and, with the purchase of coal-generated energy from ISES2, the company is at 85% *over peak demand*. Furthermore, MP&L admitted at oral argument that it is selling the less expensive energy off the system and retaining the electricity allocated to it from Grand Gulf. The Grand

Gulf electricity is estimated to have a busbar, or total generation, cost of 15¢ per kilowatt hour, compared to an average busbar cost of 4¢ for non-Grand Gulf power. Donald Lutken, the Chief Executive Officer of MP&L, testified that the company has the highest average kilowatt hour cost of the MSU system. In light of these facts, clearly the allocation of 33% of Grand Gulf power is unreasonably excessive. Since Mississippi cannot use 33% of Grand Gulf's power, the 1982 System Agreement providing for the allocation of 33% of its cost would seem to be imprudent.

The 1982 System Agreement is not the only action between MSU subsidiaries that gives us pause. The Power Purchase Advance Payment Agreement is another example of less-than-arm's-length transactions between these sister companies. We can see no benefit accruing to MP&L by entering into the agreement to pay over $74 million to MSEI in advance of receiving any power from Grand Gulf. On the contrary, this agreement could only benefit MSU and MSEI by providing funds for construction work in progress at Grand Gulf, in circumvention of our long established doctrine preventing the use of funds to finance construction work in progress from being allowed in the rate base as a basis for increase for rates. *Mississippi Public Service Commission v. Coast Waterworks, Inc.*, 437 So.2d 448 (Miss. 1983); *State, ex rel;Allain v. Mississippi Public Service Commission*, 435 So.2d 608 (Miss. 1983); *Mississippi Public Service Commission v. Mississippi Power Company*, 429 So.2d 883 (Miss. 1983). This agreement becomes especially suspect in light of the fact that it was entered among companies whose officers are controlled by MSU, the holder of all of their voting stock.

In sum, we believe that the relationship of MP&L to MSU, MSEI, and the other operating companies has brought about a situation in which Mississippi ratepayers are being intolerably burdened with high-cost nuclear energy that they neither want nor need nor can afford.

In holding that a prudency review is not precluded by federal law, we adopt the following language from *Appeal of Sinclair Machine Products, Inc.*, 498 A.2d 696 (N.H. 1985):

> The approach of this modern trend, which we here adopt and approve as being consistent with preemption doctrine applicable to State regulation of retail electric rates, is to examine whose matters *actually determined*, whether expressly or impliedly, by the FERC. As to those matters not resolved by the FERC, State regulation is *not preempted provided that* State regulation would not contradict or undermine FERC determinations and federal interests, or impose inconsistent obligations on the utility companies involved.

Id. at 704.

Several aspects of prudency have never been addressed with respect to Grand Gulf, either by state or federal authorities. Specifically, we have yet to see MP&L, MSEI or MSU justify putting Grand Gulf on line at its exorbitant cost to ratepayers. At no point in the regulatory hearings related to Grand Gulf have we found evidence from MSU or its subsidiaries of alternatives to putting Grand Gulf on line. The FERC allocations presuppose an operational Grand Gulf, delivering at, or near, full capacity. That agency was never presented with the question of whether the completion of Grand Gulf, or its continued operation, was prudent. *Mississippi Industries v. Federal Energy Regulatory Commission*, No. 85-1611 (D.C. Cir. Jan. 6, 1987) stated the issues reviewed by the FERC:

> The principal issue in ER82-616 was whether the UPSA's proposed allocation of Grand Gulf investment costs was reasonable, and, if not, how such costs should be allocated. . . . The principal issue in the System Agreement proceeding was whether FERC should approve that Agreement as filed or whether it should equalize all of part of the production costs on the system.

Id., slip opinion at pp. 20-21, 23.

Surely, it became obvious to MSU management, at least by the early 1980's, that both the cost and demand projections related to Grand Gulf were terribly incorrect. No regulatory review was made at that point, however, and management proceeded doggedly along. The Court of Appeals recognized this folly in its synopsis of the facts of this case:

> The Grand Gulf project was initiated by MSU to meet the then projected demand for electricity by the *system as a whole.* 26 FERC at 65,101-12. By the late 1970's however, it became clear that projected demand would fall well short of previous expectations. Nonetheless, MSU continued to build Grand 1 on the assumption that the overall cost per kilowatt hour would be less than that of alternative energy sources. 26 FERC at 65,102.[23]
>
> [23]This assumption is now questionable. Through the 1990's Grand Gulf will *not* produce energy that is cheaper than energy produced from alternative sources. Indeed, ALJ Liebman estimated that by 1993 ratepayers will *pay $3 billion more for Grand Gulf energy than they would for energy from comparable sources.* As of 1984 MSU was still predicting that Grand Gulf power would become economical at some future date and that at some (even later) point the project will represent a net benefit to consumers. 26 FERC at 65,103. As ALJ Liebman noted, however, the decline in the price of oil makes these projections appear rather dubious. *Id.*

Mississippi Industries, slip opinion at 16-17. However, the court made no finding with regard to prudency *because the issue was not presented.* Now that Grand Gulf is complete, at over three times its projected cost, and clearly unnecessary for the purpose of generating electricity for Mississippians, MP&L thinks that it can evade a prudency review of Grand Gulf because the plant is owned by an interstate wholesaler, which, incidentally, is wholly owned and controlled by MSU, as is MP&L. We disagree.

In remanding this case to the MPSC for a review of the prudency of the Grand Gulf investment, we rely on the expertise of this agency in making a determination of whether MSU and its subsidiaries made reasonable decisions *in light of local conditions.* We believe that this is a matter best left to this state agency to resolve, and that this issue has not been preempted by federal jurisdiction over interstate wholesale ratemaking. We, thus, agree with the following language of the Court of Appeals for the Fifth Circuit, applying the abstention doctrine of *Burford v. Sun Oil Co.,* 319 U.S. 315, 63 S.Ct. 1098, 87 L.Ed.1424 (1943):

> Given the facts before us and the structure of the Federal Power Act, which leaves jurisdiction over retail rates to the states, we conclude that the district court did not abuse its discretion in finding *Burford* abstention appropriate here. As with the regulatory scheme at issue in *Burford,* the regulation and adjustment of local utility rates is of paramount local concern and a matter which demands local administrative expertise. The regulatory scheme is complex. In addition, the Louisiana state courts are fully able to address NOPSI's complaints about Council actions: appeals from Council orders are to be filed with the Civil District Court for the Parish of Orleans. Significantly, NOPSI has not denied that adequate state court remedies exist. That the state courts often capably address claims such as that raised by NOPSI is apparent from the number of state court cases upon which NOPSI relies to prove its preemption claim substantial. Nor would federal abstention foreclose the United States Supreme Court from entertaining NOPSI's preemption claim should it wind its way up through the state courts, as is demonstrated by the path of the recent *Nantahala* case.

New Orleans Public Service v. City of New Orleans, 798 F.2d 858, 862 (5th Cir. 1986). *See also Kentucky West Virginia Gas Co. v. Pennsylvania Public Utility Commission,* 791 F.2d 1111 (3rd Cir. 1986); *Middle South Energy, Inc. v. Arkansas Public Service Commission,* 772 F.2d 404 (8th Cir. 1985).

We thus hold that the state regulatory body, in this case, the Mississippi Public Service Commission, must review the prudency of an investment such as Grand Gulf before it can enact rates based on its cost. Such a review must determine whether MP&L, MSEI and MSU acted reasonably when they construct-

ed Grand Gulf 1, in light of the change in demand for electric power in this state and the sudden escalation of costs.

II. FAILURE TO JOIN MSEI AND MSU AS PARTIES

MSU, as the owner of all of the voting stock of its operating companies, obviously controls them, as well as MSEI. The evidence shows that MP&L entered into two contracts with its sister companies—the UPSA and the advance payment agreement—which were advantageous to its sister companies and detrimental to MP&L. The result of these agreements was the August Grand Gulf bill for approximately $27 million, presented to the MPSC as evidence of the emergency need for increased rates. The substance of the bill was as follows:

To bill you for cost of service for July, 1985	$30,092,473
Less Purchase Power Advance Payment Credit	3,199,397
Net Payment	26,893,076

The MPSC was acutely aware in this case that it was dealing with transactions that were not arm's-length, yet it accepted as evidence of the reasonableness and prudency of Grand Gulf costs this bare-bones invoice. This is directly contrary to the rationale of *Western Distributing Co. v. PSC*, 285 U.S. 119, 52 S.Ct. 283, 76 L.Ed. 655 (1931), which held that state authorities had the right, despite federal regulation, to inquire into transactions between a controlling corporation and its subsidiary:

> The state authority whose powers are invoked to fix a reasonable rate is certainly entitled to be informed whether advantage has been taken of the situation to put an unreasonable burden upon the distributing company, and the mere fact that the charge is made for an interstate service does not constrain the Commission to desist from all inquiry as to fairness.

285 U.S. at 124-25, 52 S.Ct. at 284, 76 L.Ed. at 658. We do not read *Nantahala* to the contrary, although it cited with approval several cases involving purchases by closely related entities. The Court noted that "FERC's regulation still preempted review by state utility commissions of FERC approved *rates*." ___ U.S. at ___, 106 S.Ct. at 2356, 90 L.Ed. at 953-54. Neither the UPSA, which allocated more capacity to this state than it will be able to use until the mid-1990's, if ever, nor the Power Purchase Advance Payment Agreement, which was merely a conduit of construction financing from MP&L to MSEI, fall under the category of FERC approved rates. The MPSC had the authority, indeed, the duty, to inquire into the prudency of these suspect agreements.

Such a review could only be effective if MSU and MSEI (now SERI) were joined as parties. Motions were made for such a joinder and denied by the Commission. We hold that these parties should be joined in the prudency review to be accomplished on remand of this case, in order to accomplish a complete review of the transactions between MP&L, MSEI, and MSU, and their effect on Grand Gulf expense.

III. INTERVENTION OF MSU RESIDENT SECURITY HOLDERS

The only statutory basis for intervention in these proceedings is found in Miss. Code Ann. § 77-3-37(9), which allows intervenors and protestants to file direct testimony and exhibits with the MPSC. We believe that the intervention allowed in this case was error, for two reasons.

First, the security holders were already a party to these proceedings through the officers of MP&L. Shareholder intervention is improperly granted where there is no showing, as here, that the shareholders' interests are not being adequately represented. *Brieterman v. Elmar Properties, Inc.*, 507 N.Y.S. 2d 206 (N.Y.A.D.2d 1986); *Lipton v. News Intern, PLC*, 514 A.2d 1075 (Del. Supp. 1986).

Second, even under Rule 24(a)(2), Miss. R. Civ. P., intervention is only allowed under certain circumstances:

> [W]hen the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter impair or impede his ability to protect that interest, *unless the applicant's interest is adequately represented by existing parties.* [emphasis added]

See Guaranty National Insurance Co. v. Pittman, decided January 14, 1987 (not yet reported), slip opinion at p. 5. Here, the applicants' interest was obviously the preservation of their stock value through the award of a rate increase to MP&L. That interest was coexistent with MP&L's desire to enhance its financial position by obtaining a rate increase. Thus, the intervenors' interest was adequately represented by MP&L, a party to the action, and intervention of the resident security holders was improper under the facts in this case.

We, thus, find reversible error in the proceedings below, and we reverse and remand this case to the Mississippi Public Service Commission for further proceedings not inconsistent with this opinion.

REVERSED AND REMANDED.

WALKER, C.J., ROY NOBLE LEE AND HAWKINS, P.JJ., AND PRATHER, SULLIVAN, ANDERSON AND GRIFFIN, JJ., CONCUR. ROBERTSON, J., DISSENTS.

IN THE SUPREME COURT OF MISSISSIPPI
NO. 56,762

STATE OF MISSISSIPPI, EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL, ET AL.

V.

MISSISSIPPI PUBLIC SERVICE COMMISSION, ET AL.

ROBERTSON, JUSTICE, DISSENTING:

I respectfully dissent. I am of the view that our decision this day is in an area wholly preempted by authority granted by the Congress to the Federal Energy Regulatory Commission. *Nantahala Power & Light Co. v. Thornberg*, 476 U.S. ___, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986); *see also Transcontinental Gas Pipeline Corp. v. State Oil & Gas Board*, 474 U.S. ___, 106 S.Ct. 709, 88 L.Ed.2d 732 (1986).

[THIS PAGE INTENTIONALLY LEFT BLANK]

APPENDIX B

Opinion Of The Public Service Commission
Of The State Of Mississippi

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSISSIPPI

September 16, 1985

U-4620 MISSISSIPPI POWER AND LIGHT COMPANY	IN RE:	NOTICE BY MISSISSIPPI POWER AND LIGHT COMPANY OF ITS INTENTION TO CHANGE RATES APPLICABLE FOR THE RENDITION OF ELECTRIC SERVICE THROUGHOUT ITS SERVICE AREA IN WESTERN MISSISSIPPI; TO BECOME EFFECTIVE ON MARCH 1, 1985.

FINAL ORDER ON REHEARING

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSISSIPPI

September 16, 1985

U-4620 MISSISSIPPI POWER AND LIGHT COMPANY	IN RE:	NOTICE BY MISSISSIPPI POWER AND LIGHT COMPANY OF ITS INTENTION TO CHANGE RATES APPLICABLE FOR THE RENDITION OF ELECTRIC SERVICE THROUGHOUT ITS SERVICE AREA IN WESTERN MISSISSIPPI; TO BECOME EFFECTIVE ON MARCH 1, 1985.

FINAL ORDER ON REHEARING

I. Introduction

This cause came on this day to be heard by the Mississippi Public Service Commission, hereafter referred to as the "Commission", "MPSC", for final determination of the issues associated with Mississippi Power & Light Company's ("MP&L") request for a Rehearing to consider an increase in retail rates to reflect costs associated with Unit 1 of the Grand Gulf Nuclear Station ("Grand Gulf"). All other issues presented in this cause pursuant to the Notice of Intent to Change Rates filed herein by the Company, on November 16, 1984, were finally determined by the Commission in its Final Order of June 14, 1985, with the exception of prudency and rate design. See MPSC Order dated March 5, 1985. The Commission, after a rehearing had upon due notice and having considered all oral and documentary evidence presented on rehearing, finds that it has full jurisdiction of the Company and the subject matter of this proceeding. Accordingly, the Commission renders the findings and order on rehearing set forth herein.

As noted in the June 14, 1985, Final Order, this rate case constitutes the largest, most complicated, and most controversial case ever filed with the Commission. Moreover, the filing relief inherently encompasses uncertainties as to ultimate retail rate relief required relating to Grand Gulf, since the 33% allocation of Grand Gulf capacity and energy which the Company filing is based upon is being strongly challenged not only by the Commission, but by the Company itself as unjust, unreasonable, and discriminatory in its impact on the Company and Mississippi's ratepayers. In fact, the Federal Energy Regulatory Commission ("FERC") is presently considering requests for Rehearing on these very issues, and the Commission reserves the right to take any further action deemed appropriate to challenge the 33% or any other Grand Gulf allocation which the Commission considers to be legally unjustifiable for the Company and unfair to Mississippi's ratepayers.

The Commission's action addressing the complex retail issues herein which are of tremendous interest to the ratepayers as well as the Company should not in any way be interpreted by the FERC or any other party as a concession or waiver of any rights by the Commission regarding the allocation issue. The Commission intends to take every legal action available to enforce its position regarding the Grand Gulf allocation issue.

The Final Order herein constitutes an effort by the Commission to provide responsible retail rate making policy which effectively balances the interests of the Company as well as the ratepayers. The Order thus addresses the progressively worsening financial circumstances which have arisen recently for the Company since the June 14 Order, and attempts to balance the interests surrounding these circumstances with the interests of MP&L's ratepayers.

In rendering this decision the Commission is thus faced with the task of unraveling a number of extremely complex issues, for

example: (1) the fairness and appropriateness of allowing retail recovery from the ratepayers of current rates associated with a 33% allocation of Grand Gulf when the Company itself is challenging the allocation at the FERC as unjust, unreasonable, and discriminatory in its impact on Mississippi's ratepayers, (2) the fact that regardless of Company or Commission challenges to the 33% allocation, the Company is currently being billed for the power by Middle South Energy, (3) the fact that absent relief from the FERC, other legal action, or rate relief, the Company will quickly become insolvent, (4) the fact that while the Company may be seriously harmed by lack of retail rate relief at this time, the retail ratepayers will be seriously harmed by paying for an allocation which may be overturned at the FERC or through further legal action, (5) the fact that the Company got itself into its present predicament by failing to adhere to the terms of its Certificate of Public Convenience and Necessity, by agreeing to a fixed percentage allocation of Grand Gulf power and a new System Agreement when the terms of the 1973 System Agreement based on need were represented as the costs to Mississippi ratepayers associated with a permit to construct and operate Grand Gulf in Mississippi (See June 14 Order at 21 to 33.), (6) the fact that resolution of the Grand Gulf issue through litigation may not be timely enough to prevent MP&L insolvency and potential bankruptcy, and (7) the fact that absent sufficient accounting treatment for deferral of Grand Gulf related increases, minimal increases to lessen the impact on Mississippi ratepayers are insufficient to provide the Company with a menas of financing sufficient to avoid insolvency.

The Commission thus has a grave responsibility in this matter and must balance many important interests to achieve a fair result.

In reviewing the issues relating to Grand Gulf in the June 14 Order, as well as under subsequent Company requests for emergency relief, the Commission has sought to minimize and avoid

implementation of retail rates as long as possible, in hopes that the issue could be fairly and timely resolved at the FERC. Under the present circumstances surrounding this case however, the time has come for the Commission to implement certain retail rates.

The ruling of the Commission in this Final Order on Rehearing thus balances the interests of the Company and the ratepayers by providing the Company with a minimum level of current rates associated with Grand Gulf to preserve the financial viability of the Company and reliability of service, while the Commission continues to protect the interest of the ratepayers by taking every legal action available to challenge the legally unsupportable and unfair Grand Gulf allocation of FERC Opinion 234.

While this Final Order on Rehearing implements certain retail rates related to Grand Gulf, it thus controls and minimizes the impact of these costs associated with Grand Gulf while the Commission continues to pursue a reduction, if not elimination, of these costs in the future.

The Commissions' ruling allowing an increase in rates in this Final Order on Rehearing is estimated to result in current recovery in base rates of $93,768,000 over base rates approved in the Commission's June 14 Final Order in Docket U-4620 for the projected test year, the twelve months ending February 28, 1986. Fuel savings attributable to Grand Gulf Unit 1 are estimated to be $25,705,000. Therefore, the net increase in customer bills on an annual basis, after fuel savings, is estimated to be $68,063,000 or a 14.07 percent increase for the projected test year.

In this Final Order on Rehearing the Commission allows the Company a level of revenues that are estimated to result in a first year net increase in customer bills of approximately 14.07 percent over rates approved in the June 14 Final Order. A very important part of the Commission's Final Order on Rehearing is the fact

that this order requires the Company to "inventory" one-third of its allocation of Grand Gulf Unit 1 for a ten year period. MP&L's customers, if the Commission is not successful in legally challenging the FERC allocation, will not therefore begin to fully support the one-third inventoried portion of the Company's allocation of the plant until 1995.

Further, this Final Order on Rehearing requires that the Company inventory the portion of remaining cost for Grand Gulf Unit 1 that exceeds a 14.5 percent allocation for a three year period. Importantly, the result of this is the MP&L's customers will not be paying rates while litigation continues on the Grand Gulf allocation issue which the Company itself does not consider to be fair. The Company has taken the position at the FERC that any allocation in excess of 14.5% is unjust, unreasonable, and discriminatory in its impact on the Company and its ratepayers. Since it is anticipated that litigation relating to the Grand Gulf allocation issue will probably be resolved within three years the ratepayers during the next three years will not be paying in excess of what the Company itself considers to be fair and just.

This Final Order on Rehearing also requires a phase-in of that portion of the costs for Grand Gulf remaining after the inventories described above. This phase-in will result in a minimum rate increase to allow the Company to recover sufficient revenues on a current basis to continue to provide dependable and reliable electric service and to operate at a normal level of operations.

This Final Order on Rehearing addresses the Commission's findings and determinations on all issues presented by the Company's Application for Rehearing. All interested parties were afforded an opportunity to present statements and evidence on rehearing. All parties were afforded an opportunity for cross examination. After due hearings and having considered all oral and documentary evidence in this proceeding, the Commission, as discussed herein, finds and order that under the facts and unusual

circumstances of this case the Company has, on rehearing, met its burden of proof justifying its request for additional revenues related to Grand Gulf Unit 1 costs and expenses at this time.

The Commission is keenly aware of the economic conditions that currently prevail in our state and the impact of these conditions on the customers of the Company. Evidence was presented on rehearing in this cause regarding those persons subsisting on incomes below the established poverty levels and others on fixed incomes. The Commission takes judicial notice of the high unemployment in our state and, in particular, the service area of this Company. This Commission cannot ignore such testimony in reaching its decision in this case and it has been considered.

The Company proposed a senior citizen rider schedule and a low use rate schedule in its filing on November 16, 1984. The Commission directs the Company to review these efforts in light of this Order and report to the Commission on how such riders and schedules could be implemented to further reduce the impact of this Order on those persons subsisting on income below the established poverty levels and others on fixed incomes.

The law requires that the Commission balance the interests of the consumer and the utility. The Grand Gulf Unit 1 rate relief granted by this Final Order on Rehearing is an effort to balance the interests of the consumer and the utility, given current economic conditions and the facts, circumstances, and evidence in this case.

After giving due consideration to all evidence presented in Docket U-4620 related to the issue before the Commission on rehearing, including that presented on rehearing, the Commission finds that it has received and considered substantial evidence on rehearing that is material and relevant to the issue of MP&L's Grand Gulf costs and expenses and that the evidence fully supports the comments, conclusions, opinions, findings, and order

hereinafter set forth. Moreover, this Final Order on Rehearing is consistent with prior decisions of the Mississippi Supreme Court and the requirements of the Public Utilities Acts of 1956 and 1983 that this Commission's orders must be supported by substantial evidence and sufficient findings of fact.

Finally, in determining the various issues presented in this Cause, the Commission has adhered to principles of rate making consistent with prior decisions of this Commission and the Mississippi Supreme Court, but governed by the facts, circumstances, and evidence in this particular case.

II. Procedural History

The procedural history of Docket U-4620 up to the June 14 Final Order is fully set out in said order. It is appropriate to briefly summarize the procedural history subsequent to the June 14 Final Order.

On June 14, 1985, after public hearings, the Commission issued a Final Order in Docket U-4620. The June 14 Final Order allowed MP&L certain additional revenues as set out therein. However, as noted above, the June 14 Final Order denied MP& L any retail rate relief associated with Grand Gulf Unit 1.

On June 21, 1985, the Company filed rates in compliance with that portion of the June 14 Final Order that allowed the additional revenues to the Company. The Commission, by order of June 24, 1985, approved the revised rates, which went into effect on bills rendered on and after June 28, 1985.

On June 27, 1985, the Company filed an application for rehearing limited to that portion of the Commission's June 14 Final Order that denied MP&L additional revenues associated with Grand Gulf Unit 1. MP&L did not apply for rehearing on that portion of the June 14 Final Order that allowed the Company additional revenues. On July 2, 1985, this Commission granted the Company's application for rehearing.

On July 26, 1985, MP&L filed an application for emergency rates with the Commission in Docket U-4620. The emergency rate application requested that the MPSC grant emergency rates on a temporary basis, based on the Company's Grand Gulf Unit 1 costs. On August 6, 1985, the Commission set August 12, 1985, as the date for the hearing before this Commission on the Emergency Rate Application. The Commission determined that the public convenience and necessity required that the hearing on temporary emergency rates should be held on less than twenty (20) days notice. After due notice, including publication of notice in the *Clarion-Ledger* on August 9, 1985, a public hearing was begun on August 12, 1985, and concluded on August 13, 1985. At the hearing the Company presented testimony from seven witnesses. Members of the public were invited to speak and several public witnesses made statements. Testimony was also presented by Mr. James Dittmer, on behalf of the Commission Staff and by Dr. Edward Ranck and Mr. Thomas Weiss, on behalf of the Attorney General. On August 23, 1985, the Commission found it inappropriate to grant emergency rates at that time, tabled further emergency consideration, and set October 14, 1985, as the date for hearings on the Company's rehearing request.

On August 30, 1985, the Commission, upon learning that certain lines of credit for the Company had been canceled by local banks, set a final rehearing in Docket U-4620 for September 9, 1985. The Commission determined that the public convenience and necessity required that the final rehearing be held on less than twenty (20) days notice and notice of said final rehearing was duly published in the *Clarion-Ledger* on September 6, 1985.

The final rehearing was conducted on September 9 and 10, 1985, and included presentations by five Company witnesses, a witness for the Attorney General, and public witnesses. Mr. Floyd W. Lewis, the Chairman and Chief Executive Officer of Middle South Utilities, Inc. ("MSU") and Mr. Donald C. Lutken, the

Chairman and Chief Executive Officer of the Company, also testified. Mr. Thomas Weiss testified on behalf of the Attorney General.

III. Discussion and Findings Reviewing Request for Grand Gulf Related Rate Relief

As previously discussed, the rate relief sought herein is based on a strongly disputed allocation to MP&L by the FERC of 33% of the capacity and energy of Grand Gulf. The Commission, as well as the Company, has applied for rehearing of Opinion 234 by FERC, and the Commission intends to take every legal action available to challenge the validity and fairness of the FERC ruling as it applies to costs associated with Grand Gulf for Mississippi ratepayers.

The Commission has given very serious consideration to the testimony and evidence filed in Docket U-4620 relating to the issue before the MPSC on rehearing, including the rehearing testimony and evidence filed by the Company and testimony and evidence presented by others parties. In arriving at the results of this Final Order on Rehearing, the Commission gave careful consideration to the need for issuance of securities to finance the disputed Grand Gulf allocation by the FERC, the requirements for needed coverages to be able to finance, and the cash required to operate the Company at a level of operations that will assure that the Company can continue to provide reliable electric service to its customers. The rate relief granted in this Final Order on Rehearing will allow the Company to pay the disputed Grand Gulf allocation and finance any rate moderation plan. Absent the Grand Gulf Unit 1 rate relief and the deferred recovery allowed by this Final Order on Rehearing, the Company will experience a cash shortfall, short term debt will be unavailable, and the Company's bond and charter coverages will be below the minimum requirements and will preclude the Company from issuing needed mortgage debt and preferred stock to support its on going opera-

tions. The Company's securities have recently been downgraded by rating agencies as a result of Grand Gulf. Absent rate relief, the Company will shortly become insolvent.

However, while this Commission recognizes that the circumstances warrant that the Company be allowed some retail recovery of its Grand Gulf related costs, for the reasons set out below, this Commission will not allow the Company to implement Rider schedules MSE-3 and MSE-4 in conjunction with the Company proposed rate moderation schedule, Rider Schedule RM-3, which schedules together would result in an immediate 25.61 per cent increase in retail rates.

The Commission will not permit a current increase of this magnitude. There is, however, sufficient evidence, under the circumstances of this case, to support a minimum current increase in the level of operating revenues recovered through base rates and corresponding accounting treatment for the deferred Grand Gulf costs, as allowed in this Final Order on Rehearing.

A. *Circumstances Since the June 14 Order Which Warrant Grand Gulf Related Retail Relief*

Grand Gulf Unit 1 became commercially operable at 12:01 A.M. on July 1, 1985, and MP&L began actually incurring bills from Middle South Energy ("MSE") for a 33% allocation of Grand Gulf under FERC Opinion No. 234.

The Commission therefore now has before it two months of actual or historical operating data, and MSE is continuing to bill the Company for said allocation.

Company witness Brown sponsored Exhibit 139 on the MSE cost of service for July 1985 through June 1986, the first year of commercial operation of Grand Gulf 1. He testified that approximately 90 percent of the MSE cost of service is not susceptible to any measurable degree of variance. The rider schedules ordered

to be placed into effect in this Final Order on Rehearing will adjust or "true up" so that MP&L ratepayers will pay only rates based on the actual MSE cost of service.

In reviewing the request for Grand Gulf related retail relief on rehearing the Commission has thus considered the impact of the Grand Gulf costs and expenses on the Company.

Testimony was presented by F. S. York, Jr., the Senior Vice President, Chief Financial Officer and Secretary of MP&L. Mr. York testified that MP&L began receiving 33 percent of the capacity and energy from Grand Gulf Unit 1 on July 1, 1985. MP&L received a bill from MSE on Thursday, August 8, 1985, for the supply of wholesale capacity and energy from Grand Gulf Unit 1 for the month of July 1985. Exhibit 140. This bill was paid by MP&L on August 15, 1985, its due date. The total bill was $30,092,474, of which $2,234,753, being fuel costs, flowed automatically through MP&L's fuel adjustment clause during the month of July. The demand or capacity component of that bill was $27,857,721, an amount that is recovered through base rates. Another billing of $30,203,276 was rendered in September. Exhibit 142. The demand component of the August bill was $27,971,829. Similar bills will be rendered in each month hereafter, barring reversal of Opinion No. 234. MP&L's customers currently are receiving the capacity and energy associated with these billings.

Mr. York testified that MP&L's first mortgage bond coverage and preferred stock coverage have declined to levels that legally prohibit MP&L from financing its operations by first mortgage bonds or preferred stock. Also, MP&L's common equity ratio declined below 30 percent in August 1985 and will decline to 26.78 percent by November 1985, absent rate relief. MP&L is committed to the Securities and Exchange Commission ("SEC") not to issue preferred stock or first mortgage bonds if MP&L's common equity ratio is below 30 percent.

This Commission is aware that the level of coverages directly affects the ability of MP&L to finance. "Indenture coverage," also referred to as "first mortgage bond" or "interest" coverage, is the coverage requirement of the SEC that net earnings be not less than two (2) times interest requirements for present and proposed bond issues during a certain time period. "Charter coverage," also referred to as "preferred stock coverage," is an SEC requirement that net earnings be at least one and one-half (1½) times interest and preferred dividend requirements during a certain time period. York September Rehearing Testimony, pp. 16-17, 21-22.

Absent retail rates to recover Grand Gulf related costs, MP&L will have a cash shortfall of approximately $9.7 million in September, $10.4 million in October, and $18.5 million in November, for a total shortfall for the period September 1985 through November 1985 of about $38.6 million. As shown on Exhibit 122 only $20.5 million was available as of August 31, 1985, to meet this shortfall. Absent retail rate relief the Company has no source of external financing. Since June 14, Company has lost its two local lines of credit which totaled $22 million.

Preferred equity and first mortgage bonds are unavailable since MP&L went below its minimum preferred coverage level of 1.5 in May 1985 and went below its minimum interest coverage of 2.0 in August 1985, and since MP&L went below the SEC-minimum 30 percent equity ratio in August 1985.

In the absence of retail rate relief and some accounting treatment for Grand Gulf Unit 1 costs, the Company's financial situation will only worsen and its return will clearly decline over time. Thus, aside from the Commission's position which it intends to vigorously pursue regarding the allocation issue, without retail rate relief the Company will become insolvent. Under such circumstances future retail service to MP&L's customers is at best uncertain, and at worst inadequate and undependable.

In balancing the interests herein the Commission has determined it appropriate to grant certain retail rate relief under the circumstances existing upon a rehearing of this case.

IV. Grand Gulf Revenue Requirement

A. *Test Year*

In the June 14 Final Order, the Commission found that the twelve month period ending February 28, 1986, should be adopted and used as the test period in this case. In the June 14 Final Order the Commission used the projected test year ended February 28, 1986, in regard to the projected test period. The twelve months ending February 28, 1986, is hereby adopted for purposes of this Final Order on Rehearing.

B. *Jurisdictional Rate Base Including Grand Gulf*

The Company's revenue requirements associated with Grand Gulf Unit 1 are the result of purchased power expenses which are a component of operation and maintenance expenses. Thus, there is no change required in the rate base of $615,980,000 established by the Commission in the June 14 Final Order.

After considering all of the evidence, and in light of the facts and circumstances of this case, the Commission finds that this Jurisdictional Rate Base is the proper Jurisdictional Rate Base for the Company and is fully supported by the weight of the evidence in this case and said Jurisdictional Rate Base is accepted and adopted for purposes of this Final Order on Rehearing.

C. *Capital Structure*

The capital structure approved and adopted in the June 14 Final Order is not changed by recognition of MP&L's costs and expenses for Grand Gulf Unit 1. The Commission finds that the capital structure approved and accepted in the June 14 Final Order is reasonable and appropriate and adopts the same for this Final Order on Rehearing.

In its June 14 Final Order, the Commission concluded that 15.5 percent return is reasonable and appropriate for use in the case, and therefore, adopted said rate of return on equity. The overall cost of capital, resulting from the capital structure and cost of capital rates found by the Commission to be reasonable and appropriate was 11.85 percent. The Commission found this overall cost of capital to be fair, just, and reasonable in its June 14 Final Order. The level of revenues allowed in this Final Order on Rehearing will allow the Company the opportunity to earn an overall return of 11.85 percent.

D. *Jurisdictional Operating Income*

On rehearing, the Company presented an analysis of the Company operating income statement through Company witness Lubow, which operating statement gave effect to the Company's Grand Gulf related costs and expenses at a 33 percent disputed allocation under FERC Opinion No. 234. After considering all of the evidence, and in light of the facts in this case presented on rehearing, the Commission finds that the operating income statement set out below reflects the inclusion of Grand Gulf costs. The Commission thus feels that the net utility operating income as set forth below, should be used in establishing rates reflecting the FERC's disputed allocation of Grand Gulf costs.

JURISDICTIONAL INCOME STATEMENT
PERIOD II (PROJECTED TEST YEAR)
AT 33% ENTITLEMENT PERCENTAGE
OF GRAND GULF UNIT 1
AND RATES APPROVED IN JUNE 14 FINAL ORDER

TWELVE MONTHS ENDED FEBRUARY 28, 1986
($000)

	Before Increase	June 14 Final Order	MSE Cost	Total
Operating revenue				
Sales to ultimate consumers	$452,604	$48,658	$ —	$501,262
Other operating revenues	2,771	—	—	2,771
Total operating revenues	$455,375	$48,658	$ —	$504,033
Operating expenses				
O & M expenses	$503,845	$ 115	$ 326,547	$857,507
Non-firm sale to other utilities	(193,728)	—	—	(193,728)
Depreciation expenses	32,925	—	—	32,925
Taxes other than income	22,649	519	—	23,168
Income taxes	12,640	23,388	(159,028)	(123,000)
Other income & deductions	1,686	—	—	1,686
Total operating expenses	$407,017	$24,022	$ 167,519	$598,558
Net Utility Operating Income	$ 48,358	$24,626	$(167,519)	$(94,525)

E. *Revenue Requirements*

After giving due consideration to all the testimony and exhibits as indicated in the preceding paragraphs, the Commission finds that the additional revenue requirement of the Company for costs

and expenses associated with Grand Gulf Unit 1 at a 33 percent allocation is $326,547,000 as set forth below, before rate moderation plan and fuel savings. The following Summary of Revenue Requirement was presented by Company witness Lubow on rehearing. After considering the circumstances discussed herein presented on rehearing, the Commission, subject to further legal challenge to the disputed allocation through every means available, finds this additional revenue requirement to be reasonable and appropriate for the projected test year, subject to the inventory and deferrals ordered herein, and adopts the same in this Final Order on Rehearing:

MISSISSIPPI POWER & LIGHT COMPANY
SUMMARY OF REVENUE REQUIREMENT
PERIOD II (PROJECTED TEST YEAR)
AT 33% ENTITLEMENT PERCENTAGE
OF GRAND GULF UNIT 1
AND RATES APPROVED IN JUNE 14 FINAL ORDER

TWELVE MONTHS ENDED FEBRUARY 28, 1986
($000)

Rate base	$615,980
Operating income under June 14 Final Order	(94,525)
Earned rate-of-return on rate base	(15.35)%
Earned rate-of-return on common equity	(69.80)%
Required rate-of-return on rate base	11.85 %
Required operating income	72,994
Operating income deficiency	167,519
Gross revenue conversion factor	1.949317*
Revenue deficiency	$326,547

When the 11.85% rate of return is applied to the jurisdictional rate base of $615,980,000, the result is a net utility operating income of $72,994,000, which is the net utility operating income that the Company should have an opportunity to earn during the projected test year, before application of the inventory and deferral ordered herein. The level of net utility operating income that the Company is projected to earn under the level of rates approved in the June 14 Final Order is a negative $94,525,000. This produces an operating income deficiency of $167,519,000. When the appropriate tax factor is applied the Company's total revenue deficiency is established at $326,547,000.

*Conversion factor does not include city franchise tax and uncollectible accounts expense factors.

The Commission finds that based on the facts and circumstances in this record this additional level of operating revenues, recovered under the inventory, deferral, and phase-in order by the Commission below, is warranted, and will produce a rate of return sufficient to enable the Company to attract capital, to maintain its financial integrity, to cover its increased cost and provide for future adequate and dependable electric service to its customers and service areas. Further, the aforesaid level of revenues will permit the Company to maintain adequate coverage for the issuance of additional capital to provide adequate and dependable electric service.

F. *Recovery of Revenue Deficiency*

After having fully considered the evidence presented at the rehearing, this Commission is convinced that it is in the best interest of the State of Mississippi, MP&L's customers, and the Company for the Commission to allow recovery of a minimal level of Grand Gulf Unit 1 costs on a current basis. Company witness Schimpf sponsored an exhibit (Exhibit 147) that demonstrated the rate increase that the Company is requesting to recover the revenue deficiency of $326,547,000 on a current and deferred basis. Exhibit 147 reflected a net increase on current bills, after rate moderation and fuel savings, of approximately 25.61 percent increase over present rates. The Commission will not approve any current recovery that results in such a level of increase. Therefore, although the Commission does approve Rider Schedules MSE-3

and MSE-4 as ordered herein, the Commission rejects the proposed rate moderation plan, Rider Schedule RM-3, as filed by the Company.

The Commission will permit the Company to implement rates, charges, and schedules that are estimated to produce an increase in customer bills in the projected test year of approximately 14.07 percent. MP&L will be permitted to implement, effective for bills rendered on and after September 20, 1985, Rider Schedule MSE-3 and Rider Schedule MSE-4, in conjunction with Rider Schedule RM-3, as revised by this Order, to recover retail rates for MP&L's Grand Gulf Unit 1 related costs and expenses. The Company is ordered herein to file immediately a revised Rider Schedule RM-3 ("Revised Rider Schedule RM-3"), under which all costs associated with Grand Gulf Unit 1 incurred by MP&L will be recovered by MP&L as follows:

(1) Effective on September 20, 1985, and terminating on September 30, 1995, MP&L will defer or inventory the costs, exclusive of fuel costs, associated with its allocated share of the power available to MSE from Grand Gulf Unit 1, as shown in Table I set forth below, which inventory amounts are stated in terms of percentages of MSE's share of Grand Gulf Unit 1 ("Ten-Year Inventory Share"). The costs deferred and accrued in the Ten-Year Inventory Share will not be recovered from MP&L's ratepayers during the aforesaid ten-year period except as provided in this Final Order on Rehearing.

TABLE I

Year	Ten-Year Inventory Share
1	11.0%
2	11.0%
3	11.0%
4	11.0%
5	11.0%
6	11.0%
7	11.0%
8	11.0%
9	11.0%
10	

Beginning year eleven (11), the Company shall be allowed to include the balance of costs accumulated in the Ten-Year Inventory Share (which are accumulated during the period September 20, 1985 through September 30, 1995 and until such time as these costs are reflected in rates on a current recovery basis) in its rate base for determining its revenue requirements. In addition, the Company shall be allowed and permitted to amortize and recover through its rates such accumulated costs in equal annual amounts over the remaining depreciable life of Grand Gulf Unit 1 or such shorter period of time as the Commission may subsequently determine to be appropriate.

(2) In addition to the Ten-Year Inventory, effective on September 20, 1985 and terminating on September 30, 1988, MP&L will defer or inventory costs, exclusive of fuel costs, associated with its allocated share of power available to MSE from Grand Gulf Unit 1 as shown in Table II set forth below, which inventory amounts are stated in terms of percentages of MSE's share of Grand Gulf Unit 1 ("Three-Year Inventory Share"). The costs deferred and accrued in the Three-Year Inventory Share will not be recovered from MP&L's ratepayers during the aforesaid three-year period except as provided in this Final Order on Rehearing.

TABLE II

Year	Three-Year Inventory Share
1	7.5%
2	7.5%
3	7.5%

Beginning year five (5), the Company shall be allowed and permitted to amortize and recover through its rates such accumulated costs in equal annual amounts over years five through ten or such shorter period of time as the Commission may subsequently determine to be appropriate.

(3) Commencing with bills rendered on and after September 20, 1985, MP&L will be permitted to recover a portion of the costs associated with its allocated share of the power available to MSE from Grand Gulf Unit 1 on a current basis in Revised Rider Schedule RM-3, as shown in Table III set forth below, which portions are stated in terms of percentages of MSE's share of Grand Gulf Unit 1 (the "Current Recovery Share"):

TABLE III

Year	Current Recovery Share
1	14.5%
2	14.5%
3	14.5%
4	22.0%
5	22.0%
6	22.0%
7	22.0%
8	22.0%
9	22.0%
10	22.0%

A portion of Grand Gulf Unit 1 costs to be recovered from MP&L customers pursuant to this paragraph (3) will be phased in over a ten-year period in accordance with the phase-in plan set forth in sub-paragraph (a).

(a) Effective on September 20, 1985, and terminating on September 30, 1988, MP&L shall defer costs, exclusive of fuel costs, associated with its Current Recovery Share as shown on Table IV, which portions are stated in terms of percentages of MP&L's Current Recovery Share ("The Phase-in Portion").

TABLE IV

Year	Phase-in Portion
1	70.0%
2	50.0%
3	20.0%

Beginning year five (5), the Company shall be allowed and permitted to amortize and recover through its rates such accumulated costs in equal annual amounts over years five through ten or such shorter period of time as the Commission may subsequently determine to be appropriate.

The Commission estimates that the phase-in portion percentages, in combination with the inventories described in paragraph (1) and (2) and the deferral of the Rehearing Amount discussed in paragraph (4), will produce increases in customer bills attributable to Grand Gulf of approximately 14.07% in the first year, 8 to 10 percent in the second and third years, and 7 to 8 percent in the fourth and fifth years. No subsequent rate increases attributable to Grand Gulf Unit 1 are anticipated after the fifth year. At the time the Company files Revised Rider Schedule RM-3, it shall also file a calculation of aforesaid projected increases on a year to year basis.

(4) MP&L will be allowed to defer all of the costs, exclusive of fuel costs, associated with its allocated share of the power available to MSE from Grand Gulf Unit 1 incurred during the period July 1, 1985 through September 19, 1985 ("Rehearing Amount"). The Company shall be allowed and permitted to amortize on a level basis and recover through its rates such accumulated costs over years one through three or such shorter time as the Commission may subsequently determine to be appropriate.

(5) Should MSE subsequently execute a settlement agreement containing an inventory or deferral plan that results in a reduction of the charges to MP&L from that which MSE would otherwise collect relative to the disputed allocation under FERC Opinion No. 234, such reduction due to an inventory or deferral plan by MSE will first be applied on a dollar-for-dollar basis to reduce the Inventory Shares as set forth in Table I and Table II. In the event such reduction in charges to MP&L resulting from

an MSE inventory or deferral plan exceeds the Inventory Shares provided for in Table I and Table II, the allocation MP&L is allowed to recover from its customers (the Current Recovery Share) will be reduced to the extent of such excess.

(6) The Company shall be permitted to recover on a current basis the incremental cost of financing the Inventory Shares shown in Table I and Table II above, the phase-in of a portion of the Current Recovery Share described in paragraph (3), and the deferral of Rehearing Amount described in paragraph (4). The carrying charge shall be calculated by applying the incremental cost-of-money rate to the average deferred balances for each year less any tax benefits for years ending October 1, 1987, and all following years the incremental cost-of-money is defined as MP&L's before-tax weighted average cost-of-capital based on the capital structure approved in the June 14 Final Order, the cost of MP&L's most recent bond and preferred stocks sales over the preceeding 24 month period and the return on equity most recently approved by the MPSC for years ending October 1, 1986, and 1987, the incremental cost of money is defined to be 11.85%

The Commission did not approve a Rate Moderation Plan in its June 14 Final Order. This Final Order on Rehearing does, however, order the Company to implement two inventories and a phase-in plan. Although this Commission is concerned about the Company's financial condition, its primary concern is the serious harm the rate increases based on a disputed allocation have on MP&L's customers. This order thus requires deferral of a large percentage of MP&L's Grand Gulf cost. The cost of financing incurred to finance the Inventory Shares and the phase-in of a portion of the Current Recovery Share that is recovered under Revised Rider Schedule RM-3 will not be utilized to calculate the Company's cost of capital for the purpose of determining the Company's revenue requirements recovered through the Company's other rate schedules.

(7) MP&L shall have the right to sell the capacity and energy available from its Inventory Shares to third parties, without any restrictions or other requirements except that the terms of such sale cannot impose any additional costs on MP&L's ratepayers, and this Final Order on Rehearing shall consititute approval of any such sales made or to be made by MP&L from its Inventory Shares during the period through September 30, 1995. In the event MP&L is not able to sell the capacity and energy available from its inventory Shares to third parties, it shall have the right to sell the energy available from such capacity to its customers at a price equal to its avoided energy cost. Any such energy may be sold to third parties if such energy can be sold for more than MP&L's avoided energy cost.

All revenues resulting from the sale of capacity or energy from the Inventory Shares to MP&L customers or to third parties in excess of the fuel cost of producing that energy shall be applied to reduce the inventory costs associated with the Inventory Shares.

(8) The Company's inventory of a portion of the costs incurred for Grand Gulf Unit 1 (the Inventory Shares), and the Company's phase-in of the recovery of any portion of the Current Recovery Share, are contingent upon the conditions set forth below:

(a) The Company's inventory or phase-in of a portion of the Grand Gulf costs as provided in this Final Order on Rehearing is conditioned upon the Company's ability to finance such deferrals on reasonable terms. The Commission expects the Company to use its best efforts to secure such financing.

In the event the Company is not able to finance all or any portion of the Inventory Shares or the phase-in of a portion of the Current Recovery Share on reasonable terms because of (1) inadequate interest coverage ratios or other restrictions contained

in the Company's mortgage or charter and/or inability to issue debentures or other similar securities at rates comparable to mortgage debt, (2) policies, rules or regulations of the SEC, or Internal Revenue Service, (3) restrictions or requirements contained in any legislative enactments after the date of this Order which is retroactive, (4) changes in accounting standards, policies or procedures adopted by the Financial Accounting Standards Board ("FASB") or changes in the application of existing standards, policies by the FASB or (5) other restrictions upon the Company's ability to finance because of inadequate revenues or earnings, then in such event: (a) the Inventory Shares will be reduced, after thirty (30) days notice to the Commission and to all parties of record in Docket U-4620, to the extent of the Company's inability to finance the deferral of such costs on reasonable terms during the period of such inability to finance, and the percentage or amount of the costs to be recovered currently from customers (Current Recovery Share) as set forth above will be increased to the extent necessary to recover, on a current basis, the costs that would otherwise have been allocated to the Inventory Shares but for the Company's inability to finance, and (b) the proportion of the costs in the Current Recovery Share that would be deferred under the phase-in plan as set forth in Revised Rider Schedule RM-3 will be reduced to the extent of the Company's inability to finance the deferral of such cost on reasonable terms. Provided however, in the event the Commission desires a hearing on the inability to finance, the proposed reduction or adjustment may, within 30 days of such notice and by Order of the Commission, be suspended for a period of not more than 120 days and set for hearing and upon such hearing the Company shall have the burden of proof to establish the existence of such inability to finance. After proper notice and hearing before the Commission, the Company, if it meets its burden of proof aforesaid, will be permitted to amend Revised Rider Schedule RM-3 to recover such costs referred to above from its customers on a current basis.

As noted above, the Commission intends to vigorously pursue every available legal remedy challenging the validity and fairness of the FERC allocation to MP&L and the Mississippi ratepayers. Any reduction or increase in MP&L's allocated share of Grand Gulf Unit 1 from that determined by the FERC in Opinion No. 234 that results from a decision on rehearing by the FERC or any further litigation will be applied so as to proportionately reduce or increase the allocation of cost for Grand Gulf Unit 1 that is (1) inventoried by MP&L (Inventory Shares), and (2) currently recovered from MP&L customers (Current Recovery Share). Any such modification of the allocations shall be prospective unless cash refunds are required to be paid by MSE to MP&L by order of the FERC or a reviewing court. In the event such modification results in a cash refund to MP&L of payments made to MSE, the cash refund will be applied to off-set any deferral revenues.

This Order is designed to provide all the assurances currently required by the Statement of Financial Accounting Standards No. 71 (FASB No. 71). In the event there are subsequent changes to FASB No. 71, the Company may make application to this Commission to consider the effect of such changes. We authorize the Company to record the accounting entries necessary to record the Inventory Shares, phase-in of a portion of the Current Recovery Share and the deferral of the Rehearing Amount on its books of account as set out in Attachment 1. Specifically, the Company shall record the deferral of Grand Gulf Unit 1 costs in its books of account by debiting Account 186—Miscellaneous Deferred Debits and crediting Account 555—Purchased Power Expense. The amortization of costs previously deferred will be recorded by debiting Account 555—Purchased Power Expense and crediting Account 186—Miscellaneous Deferred Debits. Timing differences between the recognition of expenses for financial reporting and income tax purposes will be normalized through deferred income tax accounting.

This Final Order on Rehearing is an attempt by the Commission to achieve a result that is fair both to the Company and to the ratepayer under the circumstances of this case. As noted, under the two inventories ordered and the deferrals ordered by the Commission in this Final Order on Rehearing, ratepayers will have not supported in rates over a 14.5 percent allocation, before there is an opportunity for FERC Opinion No. 234 to be fully challenged in litigation by the parties. The Company itself has taken the position that allocations in excess of 14.5 percent are discriminatory in their impact on the Company and its ratepayers.

The Commission in this Final Order on Rehearing has established the additional revenue requirement for the Company for the projected test year as $326,547,000 which is based upon projected Grand Gulf 1 costs. In order to minimize and moderate the impact of this revenue requirement, the Commission has ordered an inventory and deferral plan, and the Commission has estimated the net effect of this plan on customers' bills for the initial year as well as several years thereafter.

G. *Burden of Proof*

In submitting a request to the Commission for a rate increase the Company has the burden of proving by substantial evidence that it is clearly entitled to the requested increase. Mississippi Public Service Commission v. South Central Bell, No. 55, 347 (Miss. 1984); State of Mississippi, ex. rel., ect. v. Mississippi Public Service Commission, 435 So. 2d 883 (1983); Mississippi Public Service v. Mississippi Power Company, 337 So. 2d 936 (Miss. 1976); and Southern Bell Telephone & Telegraph Company v. Mississippi Public Service Commission, 237 Miss. 157, 113 So. 2d 622 (1959).

While in evaluating the testimony and evidence throughout these proceedings the lack of certainty surrounding any ultimate allocation has created a tremendous problem in finding it appropriate to implement retail rates associated with Grand Gulf at

this time, a review of the undisputable circumstances brought about by the Company's financial condition since it started receiving bills from MSE, and the foregoing balancing of the interests herein, indicates that the retail relief provided herein is supported by substantial evidence.

It is important to note, however, the ruling herein is strictly limited to and based upon the evidence, facts, and most unusual circumstances associated with this case.

IT IS, THEREFORE, ORDERED BY THE COMMISSION THAT:

1. The Rate Moderation Plan contained in Rider Schedule RM-3 as filed by the Company in the September Rehearing Testimony is rejected by the Commission because it does not advance the objectives stated by the Commission in this Final Order on Rehearing.

2. Rates, charges, and schedules, designed to produce an overall increase in gross annual base rate revenues of approximately $326,547,000 over the gross annual base rate revenues approved in the Commission's June 14 Final Order will yield a fair rate of return to the Company and will be just and reasonable based upon the Company's present allocation of Grand Gulf Unit 1 as contained in FERC Opinion 234 dated June 13, 1985.

3. Rider Schedule MSE-3 and Rider Schedule MSE-4 are hereby approved and allowed, provided however Company is directed to immediately file said Rider Schedules complete as to effective dates and reflecting a definition for the term "Current Period" in MSE-4 to conform to an initial current period of September 20, 1985 through September 30, 1986 and subsequent current periods being twelve-month periods beginning each October 1 thereafter. Said Rider Schedules MSE-3 and MSE-4 are hereby ordered to become effective on bills rendered on and after September 20, 1985.

4. Company shall immediately file a Revised Rider Schedule RM-3 that shall implement the Inventory Share, the phase in of a

portion of the current recovery share and the deferred rehearing amount described in the Final Order on Rehearing, including calculations on the yearly deferrals and percentage increases. Said Revised Rider Schedule RM-3 shall be filed so as to be implemented and made effective concurrently with Rider Schedules MSE-3 and MSE-4 on September 20, 1985.

5. The Company is authorized to record the accounting entries necessary to record the Inventory Shares, the Phase-in of a portion of the Current Recovery Share, and the deferral of the Rehearing Amount, as heretofore described, on its books of account as set out in Attachment 1. Specifically, the Company shall record the deferral of Grand Gulf Unit 1 costs in its books of account by debiting Account 186—Miscellaneous Deferred Debits and crediting Account 555—Purchased Power Expense. The amortization of costs previously deferred will be recorded by debiting Account 555—Purchased Power Expense and crediting Account 186—Miscellaneous Deferred Debits. Timing differences between the recognition of expenses for financial reporting on income tax purposes will be normalized through deferred income tax accounting.

6. The Company is authorized to recover all costs deferred in the Inventory Shares of Grand Gulf costs, the phase-in of a portion of the Current Recovery Share, and the deferral of Rehearing Amounts as provided for in this Final Order on Rehearing, including paragraphs (1) through (4), and subject to the terms and conditions set out in paragraph (8).

7. The granting of rate increase relief shall be without prejudice to any and all rights asserted by this Commission in the FERC proceeding ER82-616-000 and ER82-483-000. Furthermore, this Commission will continue to pursue its litigation position before the FERC and any other appropriate legal forum.

8. For all the reasons and circumstances heretofore set out in this Final Order on Rehearing, including the present financial

condition of the Company, this Final Order on Rehearing shall be effective from and after its date of issuance.

9. The Company proposed a senior citizen rider schedule and a low use rate schedule in its filing on November 16, 1984. The Commission directs the Company to review these efforts in light of this Order and report to the Commission how such riders and schedules could be implemented to further reduce the impact of this Order on those persons subsisting on income below established poverty levels and other on fixed incomes.

10. The Company will provide to the Commission Staff on a monthly basis a calculation of monthly inventoried amounts and the carrying charges included in rates. In addition, the Company will provide the Staff all data necessary to establish the Company's ability to finance, including but not limited to, coverage ratios and bondable property on a monthly basis.

11. The effective date for implementation of the retail rates is September 20, 1985.

ORDERED by the Commission, this the 16th day of September 1985.

Chairman Snyder voted aye, Commissioner Cochran voted aye, and Commissioner Havens voted aye.

BRIAN U. RAY

BRIAN U. RAY
Executive Secretary

cc: List on File

ATTACHMENT 1
APPROVED ACCOUNTING ENTRIES FOR RECORDING INVENTORIES, PHASE-IN PLAN AND DEFERRAL OF REHEARING AMOUNT

1. The accounting entries to be recorded when the customers are actually billed under this order shall be the customer accounting entries historically authorized for MP&L.

2. Accounting entries for the Ten-Year Inventory Share of Grand Gulf costs shall be as follows:

Years 1-10

		Debit	Credit
	(1)		
Account 186	—Other Deferred Debits	$XXXX	
Account 555	—Purchased Power Expense		$XXXX

(to record inventory deferrals)

		Debit	Credit
	(2)		
Account 410.1	Provision for Deferred Income Taxes, Utility Operating Income	$XXXX	
Account 282	—Accumulated Deferred Income Taxes—Other Property		$XXXX

(to record deferred income taxes related to the inventory deferred costs)

Years 11-40

		Debit	Credit
	(3)		
Account 555	—Purchased Power Expense	$XXXX	
Account 186	—Other Deferred Debits		$XXXX

(to record amortization of the deferred cost balance in years 11-40)

		Debit	Credit
	(4)		
Account 282	—Accumulated Deferred Income Taxes—Other Property	$XXXX	

		Debit	Credit
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income		$XXXX

(to record the turn-around of deferred taxes relating to the deferred balances in years 11-40)

3. Accounting entries for the three-year inventory share of Grand Gulf costs shall be as follows:

Years 1-3

		Debit	Credit
	(1)		
Account 186	—Other Deferred Debits	$XXXX	
Account 555	—Purchased Power Expense		$XXXX

(to record inventory deferrals)

		Debit	Credit
	(2)		
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income	$XXXX	
Account 282	—Accumulated Deferred Income Taxes--Other Property		$XXXX

(to record deferred income taxes related to the inventory deferred costs)

Years 5-10

		Debit	Credit
	(3)		
Account 555	—Purchased Power Expense	$XXXX	
Account 186	—Other Deferred Debits		$XXXX

(to record amortization of the deferred cost balance in years 5-10)

		Debit	Credit
	(4)		
Account 282	—Accumulated Deferred Income Taxes—Other Property	$XXXX	

Years 5–10	(4)	Debit	Credit
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income		$XXXX

(to record the turn-around of deferred taxes relating to the deferred balances in years 5–10)

4. Accounting entries for the phase in of a portion of the current recovery share shall be as follows:

Years 1-3	(1)		
Account 186	—Other Deferred Debits	$XXXX	
Account 555	—Purchased Power Expense		$XXXX

(to record deferrals)

	(2)		
Account 410.1	—Provision for Deferred Income Taxes—Other Property	$XXXX	
Account 282	—Accumulated Deferred Income Taxes—Other Property		$XXXX

(to record deferred income taxes related to the deferred costs)

Years 5–10	(3)		
Account 555	—Purchased Power Expense	$XXXX	
Account 186	—Other Deferred Debits		$XXXX

(to record amortization of the deferred cost balance in years 5–10)

	(4)		
Account 282	—Accumulated Deferred Income Taxes - Other Property	$XXXX	

Years 5–10	(4)	Debit	Credit
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income		$XXXX

(to record the turn-around of deferred taxes relating to the deferred balances in years 5–10)

5. Accounting entries for the deferral of the Rehearing Amount shall be as follows:

September 1985			
Account 186	—Other Deferred Debits	$XXXX	
Account 555	—Purchased Power Expense		$XXXX

(to record deferral of Rehearing Amount)

	(2)		
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income	$XXXX	
Account 282	—Accumulated Deferred Income Taxes—Other Property		$XXXX

(to record deferred income taxes related to the deferral of the Rehearing Amount)

Years 1-3	(3)		
Account 555	—Purchased Power Expense	$XXXX	
Account 186	—Other Deferred Debits		$XXXX

(to record the amortization of the deferred costs)

Account 282	—Accumulated Deferred Income Taxes—Other Property	$XXXX	
Account 410.1	—Provision for Deferred Income Taxes, Utility Operating Income		$XXXX

(to record the turn-around of deferred income taxes related to the amortization of the deferred costs)

[THIS PAGE INTENTIONALLY LEFT BLANK]

APPENDIX C

Excerpts From The Federal Power Act, 16 U.S.C. §§ 791a-828c

Section 201, 16 U.S.C. § 824:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

* * *

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter, means a sale of electric energy to any person for resale.

(e) "Public utility" defined

The term "public utility" when used in this subchapter and subchapter III of this chapter means any person who owns or operates facilities subject to the jurisdiction of the Commission under this subchapter (other than facilities subject to such jurisdiction solely by reason of section 824i, 824j or 824k of this title).

* * *

Section 205, 16 U.S.C. § 824d:

Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be

made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or

charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; definition

(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are—

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

Section 206, 16 U.S.C. § 824e:

Power of Commission to fix rates and charges; determination of cost of production or transmission

(a) Unjust or preferential rates, etc.

Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affected such rate, charge, or classification is injust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order.

(b) Investigation of costs

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to

the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

Section 306, 16 U.S.C. § 825e:

Any person, State, municipality, or State commission complaining of anything done or omitted to be done by any licensee or public utility in contravention of the provisions of this chapter may apply to the Commission by petition which shall briefly state the facts, whereupon a statement of the complaint thus made shall be forwarded by the Commission to such licensee or public utility, who shall be called upon to satisfy the complaint or to answer the same in writing within a reasonable time to be specified by the Commission. If such licensee or public utility shall not satisfy the complaint within the time specified or there shall appear to be any reasonable ground for investigating such complaint, it shall be the duty of the Commission to investigate the matters complained of in such manner and by such means as it shall find proper.

APPENDIX D

Excerpts From The Mississippi Code §§ 77-3-37, 77-3-39

§ 77-3-37. Changes in rates.

(1) No public utility shall make any change in any rate which has been duly established under this chapter, except as provided in this chapter. A public utility seeking a change in any rate or rates shall file with the secretary of the commission a notice of intent to change rates. Routine changes in rates and schedules that do not involve any substantial revenue adjustment may go into effect after thirty (30) days' notice to the commission or after such shorter period of notice as the commission, for good cause shown, may allow. In all other cases, the notice of intent shall contain a statement of the changes proposed to be made in the rates then in force, the new level of revenues sought, the reasons for the proposed changes and the date proposed for such changes to become effective, which date shall not be less than thirty (30) days after the date of filing. The proposed changes may be shown by filing new schedules, by plainly indicating the changes upon schedules filed and in force at the time and kept open to public inspection or by such other manner as will clearly indicate the rates to be changed and the rates proposed. All direct testimony, exhibits and other information which any utility will rely upon in support of the proposed changes shall be filed concurrently with the filing of the notice of intent. Data, documentation and exhibits shall comply with the standard requirement list established by the commission, and such other data as the commission shall request shall be supplied by such utility.

* * *

§ 77-3-39. Hearing on rate change; suspension of proposed rates.

(1) Whenever there is filed with the commission by any public utility any notice of intent to change rates pursuant to the provisions of Section 77-3-37, the commission, if it so orders within thirty (30) days after the date such notice of intent is filed, shall hold a hearing to determine the reasonableness and lawfulness of such rate change. The commission shall hold such hearing in every case in which the change in rates constitutes a major change

in rates, as defined in Section 77-3-37. Provided, however, an abbreviated proceeding may satisfy this requirement if the commission's order is supported by the data, documentation and exhibits on file in the proceeding.

* * *

(5) If, after such hearing, the commission shall find any such rate or rates to be unjust, unreasonable or unreasonably discriminatory, or in anywise in violation of the law, the same shall be set aside, and the commission shall determine and fix by order such rate or rates as will yield a fair rate of return to the public utility for furnishing service to the public and shall make and file its conclusions and findings of facts supporting such order. A copy of such order shall be served upon the utility in the manner provided in this chapter, and the rates fixed by the commission shall be the legal rates until changed as prescribed by this chapter.

* * *

[THIS PAGE INTENTIONALLY LEFT BLANK]

APPENDIX E

FERC Opinion No. 234,
Middle South Energy, Inc.,
Docket Nos. ER82-616-000 and ER82-483-000

Middle South Energy, Inc., Docket Nos. ER82-616-000 and ER82-483-000

Opinion No. 234; Opinion and Order Setting Just, Reasonable, and Non-Discriminatory Rates

(Issued June 13, 1985)

Before Commissioners: Raymond J. O'Connor, Chairman; Georgiana Sheldon, A. G. Sousa, Oliver G. Richard III and Charles G. Stalon.

Appearances

Docket No. ER82-616-000

Elizabeth H. Ross for Missouri Public Service Commission

Hiram C. Eastland, Jr. and *Champ Terney* for Mississippi Public Service Commission

Richard M. Merriman, Robert S. Waters, James K. Mitchell, Lisa H. Powell and *William D. Meriwether,* for Middle South Energy, Inc.

Nathan Norton for Arkansas Public Service Commission

John L. Maxey and *Michael Raff* for Mississippi Legal Services Coalition

Frank Spencer and *Bill Allain* for the Mississippi Attorney General

Paul L. Zimmering, Michael R. Fontham, Marshall B. Brinkley, and *Bruce M. Louiselle* for Louisiana Public Service Commission

David N. Carne and *Peter Goldsmith* for Cities of Conway and West Memphis, Arkansas

Bernays Thomas Barclay, John B. O'Sullivan, and *Rigdon H. Boykin* for International Paper Company

Glen L. Ortman, Cliton A. Vince, and *Gregg D. Ottinger* for the City of New Orleans

Robert H. Wood, Jr. and *Linda Lipe Gleghorn* for the Arkansas Public Service Commission

Hubbard T. Saunders and *Bennett E. Smith* for the Mississippi Public Service Commission

Roger W. Giles and *Garry S. Wann* for the Office of Attorney General, State of Arkansas

Earle H. O'Donnell and *Robert R. Morrow* for Occidental Chemical Corporation

Richard M. Troy for the State of Louisiana

Charles Reusch, Robert L. Woods, James E. Rogers, Michael Small and *Maureen Thompson* for the Staff of the Federal Energy Regulatory Commission

Docket No. ER82-483-000

Richard M. Merriman, Robert S. Waters, Lisa H. Powell, William D. Meriwether, Jr., and *Floyd L. Norton, IV,* for Middle South Services, Inc.

Steve L. Riggs, Jerry D. Jackson, Robert J. Glasser, and *Carl D. Hobelman* for Arkansas Power & Light Company

Andrew P. Carter, Eugene Taggart, and *Willie J. Nunnery* for Louisiana Power & Light Company and New Orleans Public Service, Inc.

George F. Bruder, James K. Child, Jr., and *Henderson S. Hall, Jr.* for Mississippi Power & Light Company, Louisiana Power & Light Company, and New Orleans Public Service, Inc.

Robert Wood, N. M. Norton, Jr., Wallace L. Duncan, J. Cathy Lichtenberg, and *Janice L. Lower* for Arkansas Public Service Commission

Steve Clark, Garry W. Wann, Robert H. Wood, Jr., and *Roger Giles* for the Arkansas Attorney General

Richard M. Smith for the Congressional Delegations of the States of Arkansas and Missouri

Zachary D. Wilson for the Cities of Benton, North Little Rock, Osceola, and Prescott, Arkansas and Farmers' Electric Cooperative Corp.

A. Hewitt Rose, Charles F. Wheatley, Jr., Michael J. Thompson, and *Peter A. Goldsmith* for Conway and West Memphis, Arkansas

Michael E. Fontham, Marshall B. Brinkley, and *Paul L. Zimmering, Jr.* for Louisiana Public Service Commission

David B. Robinson and *Mariano G. Hinojosa* for Louisiana Attorney General

David B. Robinson for Louisiana Congressional Delegation

Honorable W. J. (Billy) Tauzin for W. J. Tauzin

Clinton Vince, Glen Ortman, Paul Nordstrom, and *Greg Ottinger* for the City of New Orleans

Champ Terney, Hiram C. Eastland, Jr., Bennett Smith, Glen Hays, Donna Allday, Edwin Lloyd Pittman, and *Jay Stewart* for Mississippi Public Service Commission

John L. Maxey, II for Mississippi Attorney General

Honorable Wayne Dowdy and *Webb Franklin* for Wayne Dowdy and Webb Franklin

Martin C. Rothfelder for the Missouri Public Service Commission

James M. Fisher and *Richard W. French* for the Missouri Office of the Public Counsel

James B. Selna, David T. Beddow, and *Donald T. Bliss* for Amax

John B. O'Sullivan, Robert F. Shapiro, and *Bernays T. Barclay* for International Paper Company

Earl H. O'Donnell and *Robert R. Morrow* for Occidental Chemical Corp. and Georgia Pacific Corp.

Paul H. Keck and *Brian R. Gish* for Mississippi Industries

Alfred J. Cheplin, Jr. for Mississippi Legal Services Coalition

Bonnie S. Blair and *Robert McDiarmid* for Municipal Energy Agency of Mississippi

John Nassikas, James L. Trump, J. Mark Davis, Alston Jennings, Jr., and *Kenneth A. Barry* for the Arkansas Industries

William A. Chesnutt and *Henry R. MacNicholas* for Union Carbide Corp.

Thomas L. Blackburn and *Charles Reusch* for the Staff of the Federal Energy Regulatory Commission

Pending before the Commission are briefs on exceptions to two initial decisions in dockets which are not consolidated but which have overlapping issues concerning the appropriate allocation of capacity costs incurred on the Middle South Utilities (MSU) system. Docket No. ER82-483 involves a 1982 System Agreement which sets forth the terms and conditions for transactions among MSU's four wholly owned subsidiaries, Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (MP&L), Arkansas Power & Light Company (AP&L), and New Orleans Public Service, Inc. (NOPSI). Docket No. ER82-616 involves a Unit Power Sales Agreement under which Middle

South Energy, Inc. proposes to sell to LP&L, MP&L, and NOPSI all of the capacity and energy from its Grand Gulf Nuclear Station located in Port Gibson, Mississippi.[1]

The initial decision in ER82-616 was issued on February 3, 1984. 26 FERC ¶ 63,044. The initial decision in ER82-483 was issued on February 4, 1985. 30 FERC ¶ 63,030. This opinion addresses both initial decisions. Section I addresses the major cost allocation issues contained in both dockets, Sections II and III separately address the remaining rate issues, except for rate of return, in each of the dockets, and Section IV addresses rate of return for both dockets.

At the outset, we emphasize that these dockets present some extremely difficult and controversial cost allocation issues which have no easy answers. There appears to be no proposed resolution in the records that would please all parties. We therefore wish to express our disappointment in the fact that, despite every encouragement and opportunity, the parties were unable to unanimously resolve their differences. We have reached a decision which we believe will achieve an equitable result and is supported by the records. That decision is to approve the 1982 System Agreement as filed in Docket No. ER82-483 (with the exception of certain

[1]Also pending before the Commission is a proposed settlement agreement filed on January 4, 1985, as revised on February 5, 1985, by AP&L, LP&L, MP&L, NOPSI, Middle South Energy, Inc., and Middle South Services, Inc., seeking to resolve all issues in the two dockets. Comments on the settlement were received from 22 participants, almost all of whom opposed the settlement as filed but indicated that they favored resolution of the proceedings by settlement. On February 22 [30 FERC ¶ 61,196], the Commission issued an order appointing a three-judge panel to preside over further settlement negotiations. The three-judge panel reported to the Commission on March 14, 1985, that further settlement procedures at that time would be fruitless, and that the Commission should go forward with its decision. The January 4, 1985 settlement, as revised on February 5, 1985, is hereby rejected.

small modifications addressed in Section III, *infra*), and to adopt the Grand Gulf allocation recommended by the presiding judge in Docket No. ER82-616.

I. Grand Gulf Allocation and Production Cost Allocation

This section contains a general description of the two dockets, the initial decisions, the major legal, factual, and policy issues raised concerning cost allocation, an analysis of the facts and arguments, and a resolution of the issues raised. The reader is referred to the initial decisions for further background information.

A. Docket No. ER82-616 (Grand Gulf Agreement)

The major issue in Docket No. ER82-616 is who among the four MSU operating companies should bear the costs of the Grand Gulf Nuclear Electric Station, and in what proportions. Grand Gulf is located in Port Gibson, Mississippi. When completed, it will consist of two 1,250 MW generating units. Unit No. 1 (Grand Gulf 1) is expected to begin commercial operation on July 1, 1985. Unit No. 2 (Grand Gulf 2) is not expected to begin operation until 1989.[2]

Ninety percent of the Grand Gulf units is owned by Middle South Energy, Inc. (MSE), a wholly owned subsidiary of MSU.[3] The units were originally planned by MP&L, but MSE was created to facilitate the financing of the units when MP&L determined that it would be unable to do so. This docket began when

[2]Unit No. 1 was previously scheduled to begin commercial operation in the first quarter of 1985. On May 23, 1985, the Commission was notified by letter from MSS that the unit is now scheduled to begin commercial operation at 12:01 on July 1, 1985. Construction of Unit No. 2 was suspended in 1979 pending completion of Unit No. 1, and the system has not reached a decision as to when it will commence construction of Grand Gulf 2. (26 FERC at p. 65,122.)

[3]MSE sold 10% of Grand Gulf to the South Mississippi Electric Power Association.

MSE filed a Unit Power Sales Agreement (UPSA) which provides for the sale of the output of both nuclear units for their lives under a formula, or cost of service, rate for determining the price of Grand Gulf's output. Under the agreement, all of the output of both units would be sold to LP&L, MP&L, and NOPSI according to certain entitlement percentages. The entitlement percentages for Unit No. 1 would be: LP&L—38.57%; MP&L—31.63%; NOPSI—29.80%. Although all four MSU operating companies are signatories to the UPSA, none of the output would be sold to AP&L under the agreement as initially proposed.

The major objection of the numerous intervenors in the docket concerns MSE's decision to sell all of Grand Gulf's output only to LP&L, MP&L, and NOPSI, and none to AP&L. The costs of Grand Gulf are enormous. The cost of MSE's 90% share is estimated at approximately $3 billion, resulting in a cost per kW of approximately $2,500. LP&L, MP&L, NOPSI, and their customers want AP&L to share some of the burden of these costs.

The Initial Decision

Presiding Judge Liebman concluded that the evidence was overwhelming that the Middle South system is a single integrated and coordinated electric system operating in Louisiana, Mississippi, Arkansas, and Missouri. He found that the Grand Gulf project was initiated in the 1970's to meet the then projected load demand of the *system* and not just the load of any Middle South operating company or companies, and further that every unit on the Middle South system had been constructed to meet system load. Therefore, he concluded that the costs of Grand Gulf capacity and energy should be shared equitably by all four operating companies and their customers.

After finding MSE's proposed entitlement percentages unjust, unreasonable, and unduly discriminatory, the judge adopted the

allocation proposal of the Louisiana Public Service Commission (LPSC) and Occidental Chemical Corporation (OCC). Under their proposal, each operating company would be allocated a share of the cost of nuclear capacity on the MSU system roughly in proportion to each company's relative share of system demand.[4] The Grand Gulf allocation percentages adopted by the judge, contrasted to those proposed by MSE, are:

Entitlement Percentages—Unit No. 1

Company	*As filed by MSE*	*As recommended in Initial Decision*
AP&L	-0-%	36.00%
LP&L	38.57	14.00
MP&L	31.63	33.00
NOPSI	29.80	17.00
	100.00%	100.00%

The effect of the judge's decision was not just to allocate Grand Gulf costs, but to allocate the costs of all nuclear capacity on the MSU system. The judge also concluded that the costs of Grand Gulf Unit No. 2 should not be included in the automatic adjustment clause of the UPSA since completion of the unit and its costs are speculative, and the rationale for allocating costs of that unit may be different when the unit is completed.

Exceptions to the initial decision were filed by the following participants: the State of Arkansas, Arkansas Industries, AP&L, the Arkansas Public Service Commission (APSC), the Cities of Benton, North Little Rock, Osceola, and Prescott, Arkansas, and the Farmer's Electric Cooperative Corporation, the Congressional Delegations of Arkansas and Missouri, the Cities of Conway

[4]Two other proposals, in addition to MSE's, were also before the judge. The Mississippi Public Service Commission had proposed that the Grand Gulf allocation be based on the 1973 System Agreement, with Grand Gulf deemed to be a participation unit. (The operation of the 1973 Agreement is discussed *infra*.) The City of New Orleans proposed allocating Grand Gulf power based on the present peak demands of the MSU operating companies.

and West Memphis, Arkansas, International Paper Company, the Louisiana Public Service Commission (LPSC), the Mississippi Public Service Commission (MPSC) and Mississippi Attorney General, Mississippi Legal Services Coalition, the Missouri Public Service Commission, the City of New Orleans (CNO), Occidental Chemical Corporation, MSE, and the Commission Trial Staff.

Because the briefs are so numerous and many of the exceptions are repetitive or overlap, we will not enumerate the exceptions of every party. Rather, the following description categorizes the participants according to their general positions on exceptions regarding the Grand Gulf allocation issue. Also, because many of the exceptions in this docket overlap with those in ER82-483, they will be stated only briefly here and are described in greater detail in the discussion of ER82-483. Arguments made in briefs opposing exceptions in both dockets are not described separately because they generally repeat arguments previously made; where they do raise something new, they are discussed where appropriate in the opinion.

Mississippi Parties

The MPSC, Mississippi Attorney General, and Mississippi Legal Services Coalition claim that the judge's ruling is based on numerous erroneous factual and legal conclusions, and will have an unduly discriminatory impact on Mississippi ratepayers. They assert that the decision undermines the MPSC's determination pertaining to the need and economic justification for Grand Gulf when it granted a certificate to build the plant in its State. Lastly, they claim that the decision violates the doctrine of equitable estoppel since the MPSC relied on representations, made in the State certificate proceedings, that excess Grand Gulf capacity would be sold to the other operating companies.

Arkansas Parties

The Arkansas participants, joined by the Missouri participants, are major objectors to the judge's Grand Gulf allocation. They claim that the Commission has no jurisdiction to compel MSE to sell or AP&L to purchase Grand Gulf power, particularly since MSE is not a jurisdictional utility and AP&L has no contractual responsibility to purchase power under the UPSA. The *Mobile-Sierra* doctrine,[5] they assert, precludes alteration of the voluntary UPSA absent unusual circumstances.

The APSC specifically contends that an order requiring AP&L to purchase Grand Gulf power from MSE would improperly intrude on its regulatory authority regarding retail rates and the necessity for plant construction. If the Commission does have the authority to compel AP&L to purchase power, the APSC claims that it is inappropriate to exercise such power here.

The Arkansas participants further argue that the judge erred in finding the filed UPSA to be unjust, unreasonable, and unduly discriminatory. A major error by the judge, they state, was his analysis of the retail rate impact of various allocations, and his failure to analyze allocation from the standpoint of the *need* for Grand Gulf power. They also dispute the judge's findings that generation on the system has been planned to serve the system as an integrated entity, and that one of the system's goals was to equalize generating costs.

Louisiana Parties

The Louisiana parties other than CNO do not object to the judge's Grand Gulf allocation. CNO excepts to the judge's failure to accept its proposal to allocate power and related costs among the four subsidiaries based on each company's current relative peak demand.

[5] *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*); and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*).

Middle South Energy, Inc.

MSE's exceptions to the initial decisions concern issues other than the specific Grand Gulf allocation percentages for the operating companies.

Commission Trial Staff

The Trial Staff's exceptions also are to issues other than the specific Grand Gulf allocation percentages for the operating companies.

B. Docket No. ER82-483 (System Agreement)

The System Agreement which is at issue in Docket No. ER82-483 sets forth the terms and conditions for transactions among the four MSU operating companies, including the sale and exchange of capacity and energy. Transactions among the companies have been controlled by some form of system agreement for over 30 years, with three similar agreements in all—the 1951, 1973, and 1982 versions. This docket involves the 1982 version filed by Middle South Services, Inc. (MSS), the service company subsidiary of MSU.

The system agreements have provided the contractual basis for planning and operating the companies' generating units on a single-system basis, and also have provided a basis for equalizing certain cost imbalances that result from this method of planning and operating the units. How the previous agreements have done so is as follows. If a company was responsible for 30% of the system's demand, it became responsible for 30% of the system's capacity. If the company's owned or purchased capacity was more than 30% of the system's capacity, the company was said to be "long" and received payments from the other companies for the difference. If the company's owned or purchased capacity was less than 30% of the system's capacity, it was said to be "short" and had to make payments to the others.

Under the 1973 System Agreement, payments from the short to the long companies were based on the costs of the long company's most recently installed generating unit. The 1982 System Agreement, as filed, would change the basis on which payments are made by the short to the long companies. Rather than basing payments on the capacity costs of the long companies' most recent generating units (nuclear and coal-fired units), it would instead base them on the capacity costs of the long companies' intermediate units (oil and gas-fired units). This change constitutes the major dispute in the case. The change supposedly was made on the basis that, due to their fuel costs, the older units now have operating characteristics directly related to use as "reserve" capability, and it is only reserve capacity that is to be equalized under the System Agreement.

Four other allocation methodologies were proposed in this docket but, because several of them are similar, there are actually only a total of three basic proposals before the Commission:

(1) MSS's proposal, above, to equalize reserve capacity costs only, based on the cost of the long companies' older oil and gas-fired generation units;

(2) the Mississippi Public Service Commission's (MPSC) proposal to equalize reserve capacity costs only, based on the cost of the long companies' most recent generation units, and to make MSE a party to the System Agreement; and

(3) proposals by the Commission Trial Staff, the LPSC, and CNO to equalize all or part of the system's production costs.[6]

[6]Three variations of production cost equalization were presented: (1) the Commission Trial Staff proposed to equalize the costs of all base load (coal and nuclear-fired) facilities on the basis of each company's annual average load to the average annual load of the system, and to levelize all carrying charges for the base load units; (2) the LPSC proposed to combine all production costs (not just base load), and allocate them based on each company's capability responsibility; and (3) CNO proposed to equalize all base load units, but also to allocate the remaining production units, including peaking units, on a two-part basis by which capacity costs would be treated as set out in MSS-1 of the 1982 System Agreement and energy would be drawn from the system pool.

MSS's proposal was supported by AP&L, the Arkansas Public Service Commission, and other Arkansas parties, as well as the Missouri Public Service Commission and Missouri Public Counsel. The production cost equalization proposals would have substantial impact on the ratepayers represented by these parties. According to Staff's initial brief, AP&L would pay $163 *million more* in 1984 under the LPSC proposal than under the MSS proposal, and $228 *million more* under the Staff proposal than under the MSS proposal (excluding consideration of Grand Gulf or any decrease in AP&L's projected coal transportation expenses).

As for the MPSC proposal, it would have the effect of making the Grand Gulf units participation units, since they are the only units owned by MSE. Grand Gulf's capacity costs, which carry energy entitlements, would thus shift among the individual companies as the companies become short or long, and the short companies would end up paying for Grand Gulf's capacity and energy costs. Because MP&L is a long company and is expected to remain so until the 1990's, it would avoid any responsibility for Grand Gulf during that time.

The Initial Decision

Presiding Judge Head thoroughly analyzed and discussed the Middle South System, as well as the arguments for and against production cost equalization. His major findings and conclusions are as follows.

(1) While this Commission has the power, from a jurisdictional standpoint, to order production cost equalization, such power must be exercised with caution since it will have a substantial impact on the retail ratemaking ability of the States involved. (For example, approval of the Staff proposal would subject more than 75% of rate base to our jurisdiction, and an even greater percentage of the operation and maintenance expenses, thus leaving the States with little control over the absolute level of retail rates.) The case law concerning State/Federal jurisdictional disputes and the legislative history of the Federal Power Act support a finding that Federal regulation is meant to be supplemental to, not in place of, State regulation. Therefore, this Commission's exercise of overlapping jurisdiction must be tempered and weighed against the policy consideration that generation facilities and retail rate regulation should be left to the State commissions.

(2) The policy to encourage voluntary pooling, contained in the Federal Power Act (FPA) and Public Utility Regulatory Policies Act (PURPA), cannot operate to block the Commission's power under Section 206(a) of the FPA to reallocate costs and expand the scope of power pooling transactions, if to do so is necessary in the public interest.

(3) Although adoption of any one of the various production cost allocation proposals would result in substantial savings to various companies, none of the cost differentials or impacts are of such magnitude that they *per se* require adoption of one proposal over another. These impacts are a factor to be taken into account in determining a just and reasonable system arrangement.

(4) Characterizations by this agency and others that the Middle South System is a closely integrated and coordinated power pool do not specifically dictate that production cost equalization must be ordered.

(5) The MPSC's proposal (retention of the 1973 System Agreement) is not just and reasonable. It would result in the short companies (LP&L and NOPSI) paying approximately $3 billion for the Grand Gulf costs for a 10-year period, after which time MP&L would become short and then enjoy its share of the unit in the less expensive years (after it has been initially depreciated). The proposal also would not tend to achieve the System Agreement's stated goal of each of the operating companies diversifying its fuel mix.

(6) The record establishes that the Middle South companies constitute a highly integrated electric system, with common planning and central dispatch, for the purpose of achieving economies of scale and enhanced reliability. However, the evidence also reveals a pattern of autonomy, particularly as to specific plant site locations, fuel, and financing. The MSU companies have never been operated as a single system where all the generation is shared and responsibility therefor is allocated to the operating companies. To revise the 1982 System Agreement by ordering production cost pooling and equalization would constitute a drastic deviation from past system practices relating to intercompany transactions, and would change the underlying nature of such operations. It would amount to a revision of the Middle South System in a manner not consistent with the history of operation on the system, which reveals a pattern of autonomy on the part of the individual operating companies, and indicates that generation additions other than Grand Gulf were made primarily to satisfy individual company needs. Production cost equalization is not warranted at this time. The 1982 System Agreement should be approved with regard to its reserve equalization provisions.

(7) Grand Gulf, however, is an anomaly to the regular planning and construction of generating facilities on the system and, unlike other units, it *was* planned, licensed, and constructed as a *system* plant, by a separately created entity, and was intended to supply power not only in Mississippi, but throughout the entire MSU system. As such, the financial responsibility for Grand Gulf should be borne by all the operating companies. Grand Gulf should be integrated into the 1982 System Agreement by having each of the four operating companies pay for the production costs of that facility based on the ratio that the individual operating company's total annual demand bears to the total system annual demand. This ratio would be calculated at the close of the calendar year.

To integrate Grand Gulf responsibility into the 1982 System Agreement, the judge concluded that each operating company's share of the unit could be treated as part of its capability under

Section 2.14 of Article II, as an input in MW available under contract from a supplying source. As such, it would affect each company's capability and become part of the reserve equalization calculation. Thus, the Grand Gulf share would be taken into account in determining which company is long or short.

The judge stated that although a precise calculation had not been made, his proposed treatment of Grand Gulf should result in economic differences at about the midpoint of those shown for the 1982 System Agreement and the equalization proposals. The net effect is that Grand Gulf would be equalized but LP&L's Waterford 3 nuclear unit would not. (According to a March 18, 1985, article in *The Wall Street Journal,* Waterford 3 was to be in commercial operation during the second quarter of 1985.)

On February 8, 1985, MSS filed a motion requesting clarification of the initial decision, seeking a definition of the terms "individual operating company's total annual demand" and "total system demand." On March 6, 1985, the judge issued an order denying the motion for clarification, but stating that the APSC's interpretation of the unclear terms was correct. The APSC, in its response to the motion for clarification, had suggested that the terms refer to the total annual kilowatt-hours used by an operating company (individual operating company's total annual demand) and the total annual kilowatthours used by the Middle South system as a whole (total annual system demand), with off-system sales excluded from both terms.

Exceptions to the initial decision were filed by the following participants: MSS, MP&L, AP&L, LP&L and NOPSI, the Mississippi Public Service Commission and Mississippi Attorney General, the Louisiana Attorney General, the Governor of Louisiana and Louisiana Department of Natural Resources, the Louisiana Public Service Commission, Union Carbide Corporation, Occidental Chemical Corporation and Georgia Gulf Corporation, the City of New Orleans, Jefferson Parish, Louisiana, the

Arkansas Public Service Commission joined by the Missouri Public Service Commission and Missouri Public Counsel, the Arkansas and Missouri Congressional Delegations, AMAX, Inc., International Paper Company, Arkansas Industries, the Arkansas Attorney General, and the Commission Trial Staff.

As was done with the ER82-616 exceptions, the following description categorizes the participants according to their general positions on exceptions.

Mississippi Parties

The MPSC and Mississippi Attorney General (MAG) claim that the judge's decision is outside the scope of the Federal Power Act and ignores the dual regulation of electric utilities by State and Federal government. The MPSC granted a certificate to MP&L to construct Grand Gulf in reliance on representations that the Grand Gulf units would become participation units under the System Agreement, and that none of the additional capacity costs of the units would be allocated to MP&L in excess of its area demand requirements. Citing recent Supreme Court authority for the proposition that the States retain traditional authority over decisions as to the need and economic feasibility of additional generating capacity,[7] the MPSC and Attorney General contend that the initial decision undermines such State authority. They further argue that it violates the doctrine of equitable estoppel, since the MPSC detrimentally relied on the representations of MP&L and MSE, as agents for the MSU system, concerning allocation of Grand Gulf costs.

The MPSC and MAG further contend that the initial decision will have a chilling effect on future multi-state cooperation in constructing additional generating capacity for future needs. They pose the question of why a reasonable State commission would

[7]*Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Comm'n*, 461 U.S. 90 (1983).

grant a company's request to build additional capacity if that commission had no assurances as to the disposition of costs associated with capacity beyond what is needed to serve the requesting company's customers.

MP&L is currently a long company. The MPSC and MAG argue that the 1982 System Agreement would require MP&L to subsidize capacity-deficient operating companies because it would require MP&L to take and pay for the high costs of Grand Gulf, yet sell its excess generation based on the low cost of its oil and gas units.

The MPSC and MAG continue to advocate the participation unit concept as being in harmony with the legal policy that the States retain authority regarding the need for and economic feasibility of additional capacity, and in harmony with the history of the MSU system operation which has encouraged State approval of generating capacity on the system.

Other Mississippi parties are not aligned with the MPSC and MAG. The Mississippi Congressional Representatives, MP&L, and Mississippi Industries support the ER82-483 initial decision. If that initial decision is not adopted, however, they support production cost equalization. MP&L previously supported system-wide production cost equalization, but in its brief on exceptions states that it has now concluded that the initial decision in ER82-483 more accurately reflects the history and operation of the MSU system than does the initial decision in ER82-616, and that it reaches a just and reasonable result.

Arkansas Parties

Because so many exceptions and arguments are raised by the various Arkansas interests, the major ones are enumerated individually below:

(1) The judge in this proceeding had no authority to allocate Grand Gulf costs. The scope of this docket was specifically limited to the System Agreement. MSE is not a party to the System

Agreement and was not a party in this docket. The Grand Gulf allocation issue is solely within the scope of ER82-616, and consolidation of the two dockets was previously denied.

(2) The Commission has no jurisdiction under the FPA to require AP&L to purchase or MSE to sell Grand Gulf power. Although the judge and some parties use the term "allocation," the judge's decision in effect constitutes a forced purchase and sale, since it would require MSE to sell and AP&L to buy 33% of Grand Gulf, and AP&L to sell an equivalent amount of its own coal and nuclear power. To compel AP&L to purchase capacity and enlarge its generating capability violates Sections 201(b), 202(b), and 212(a) of the FPA.

(3) Grand Gulf was not, as the judge held, planned for system use. The record shows that it was built only for those companies anticipating a deficiency in coal and nuclear capacity. AP&L was not one of those companies. Further, the system never had a goal to equalize costs.

(4) The judge improperly found that the Commission has jurisdiction to order production cost equalization. The *Mobile-Sierra* doctrine precludes overturning the voluntary 1982 System Agreement unless there is an uneqivocal public necessity to do so. Although the Commission may have authority to *modify* the transactions and rates proposed under the System Agreement, it cannot substitute dramatically different transactions since the statutory scheme provides for regulation of *voluntary* transactions. Jurisdiction is given under Section 201 of the FPA, and Section 206 cannot be used to overstep this jurisdictional authority.

(5) Equalization of Grand Gulf or other production costs would result in unauthorized Federal regulation of rate base and of generating facilities. Requiring AP&L to buy Grand Gulf or other capacity would change the retail rate base because it results in a transfer of rate base from other utilities to AP&L. It would

also shift generation from one utility to another. The States would be required to allow pass-through of these costs in retail rates, thereby being forced to relinquish a critical aspect of State regulation, i.e., determination of what fixed and operating costs of generating facilities should be allowed. Under production cost equalization, a State commission would be forced to approve charges that derive from plants which it did not approve, which are outside its jurisdiction, and which were not needed to meet the needs of the State's ratepayers.

(6) Equalization of costs would conflict with representations to the APSC during certification proceedings that AP&L's plants were necessary to meet AP&L peak load within its own system, and that plants would be maintained and operated by AP&L to meet native load requirements.

(7) The judge's findings regarding production cost equalization could frustrate Section 202 of the FPA, and Section 206(b) of the PURPA, under which the Commission is to encourage voluntary power pooling and coordination.

(8) Assuming that the Commission has jurisdiction to reallocate Grand Gulf costs, the judge erroneously failed to consider and credit the operating companies for their existing capacity. For example, a substantial amount of AP&L's current base load energy is going to benefit the pool since AP&L will have excess capacity into the 1990's, even absent Grand Gulf. If AP&L were allocated Grand Gulf capacity, it would be unable to use any of the Grand Gulf energy and the forced Grand Gulf purchase would also go to benefit the pool. In other words, AP&L would be forced to buy capacity it can't use. Any allocation must consider need as well as current demand.

(9) Production cost equalization in this case would have nationwide implications and would inhibit power pooling. MSU pooling practices are typical of numerous pools in the country,

and none of the other pools have ever equalized total capacity costs. Facilities with low operating and construction costs would attempt to withdraw from existing pools or refrain from entering new ones. Pool members would be uncertain as to future cost stability and unable to plan accurately for load growth, sales, and capacity construction. It could also impair a pool member's ability to raise capital. A utility forced to purchase additional capacity might not be able to recover the additional costs through increased rates right away because of regulatory lag, and this could have an adverse financial impact on the company.

(10) Production cost equalization would inhibit the States in granting power plant certificates. They would be unable to balance the need for the plant in a particular State because it would never be used solely for native load.

(11) Production cost equalization would undermine the goals of the System Agreement, particularly Section 3.05, which says that a long-term goal is for each company to have a proportionate share, not a proportionate sharing, of base load units to meet native load.

(12) Production cost equalization would conflict with the Public Utility Holding Company Act (PUHCA). It would undermine the SEC's authority because it would ignore the separate identities of the operating companies. The main purpose of the PUHCA was to reduce the size and simplify the structure of affiliated utility systems so that they could be regulated by local authorities. Production cost equalization would frustrate this.

(13) If the 1982 System Agreement is found unjust, unreasonable, unduly discriminatory, and unequivocally against the public interest, then the burden is on those opposing the 1973 System Agreement to show that it should not be reinstated.

The Arkansas interests continue to support the 1982 System Agreement as filed, claiming that it meets the system goals of moving each company toward a proportionate ownership of coal

and nuclear capacity, and reducing each utility's fuel costs. The APSC, however, states that if the 1982 Agreement is rejected, the Commission should reinstate the 1973 System Agreement but amend it to state that units owned by MSE but sold to individual operating companies may qualify as participation units for determining a company's capability.

Arkansas Industries also suggests that if the 1982 System Agreement is not accepted as filed, there are several options available other than production cost equalization. These include retention of the 1973 Agreement, with Grand Gulf treated as a participation unit and a levelization of the high front-end costs as to LP&L and NOPSI, or requiring joint ownership of Grand Gulf by looking through MSE and assigning the plant to the rate bases of the companies as though the plant were jointly owned. Noting that the January 5, 1985 proposed settlement in these dockets recognized the shareholders' responsibility to absorb some of the costs of a new, extraordinarily expensive plant that no one wanted, International Paper contends that if the Commission does allocate MSE capacity through the System Agreement, then it must allocate a substantial portion to the Middle South shareholders.

Louisiana Parties

The Louisiana participants all support some form of cost equalization, but vary somewhat in their exceptions and in what they are willing to accept. Their major exceptions follow, with major areas of disagreement specifically noted.

(1) The initial decision will result in LP&L bearing 100% of the expensive Waterford 3 costs, and 41% of Grand Gulf costs. The costs of these two units together will equal more than the total net plant investment in the entire system in 1981, and the effect of the decision is undue discrimination against LP&L.

(2) The testimony and documentary evidence show that *all* generation additions on the MSU system have been planned and operated on a systemwide basis, and that there is no distinction between Grand Gulf 1 and Waterford 3. The judge's finding of autonomy is not supported by the record and conflicts with his earlier findings regarding the integrated nature of the system. The evidence shows that all critical decisions regarding plant additions are made by and for the system as a whole.

(3) Some form of production cost equalization is necessary to avoid undue discrimination on the system. This is because the filed System Agreement creates enormous cost disparities that are based only on accidents of timing in decisions as to the building of plants for the entire system.

(4) Production cost equalization would not result in an undue extension of Commission jurisdiction. The judge misunderstood its impact. His finding that 75% of AP&L's rate base would be moved from State to Federal control is incorrect and ignores the fact that even in the absence of production cost equalization, the Commission would be required to exercise jurisdiction over a substantial portion of these costs. Also, the judge's analysis is flawed in that the issue here is discrimination in rates at the *wholesale* level, yet he relied on evidence as to revenue per kWh at the *retail* level and failed to recognize legitimate cost-based differences at the retail level.

(5) Production cost equalization would not be a dramatic departure from past system operation, as found by the judge. The overall pattern of generation additions shows that capacity was added to benefit the system as a whole, and that previous system agreements achieved an approximate equalization of production costs. Additionally, equalization would achieve the basic objective of the System Agreement to equalize any imbalance of costs of facilities used for the mutual benefit of the companies.

(6) The judge erred in making any allocation of Grand Gulf in this docket, since the issue was reserved for ER82-616 and consolidation of the two dockets was denied.

(7) The judge was obligated to respond to allegations that the 1982 System Agreement is not just and reasonable, and failed to do so.

(8) The judge ignored the proposal of LP&L, NOPSI, and MP&L to consider a phasing-in of production cost equalization over a three-year period. This would avoid the need for future *ad hoc* adjustments based on changed circumstances, and would permanently solve the problems presented in this case.

Some of the Louisiana parties assert the following alternative positions if production cost equalization is not adopted:

(1) The LPSC and Attorney General of Louisiana state that if production cost equalization is not adopted, then the initial decision should be overturned as to Grand Gulf and the ER82-616 allocation adopted, but using updated cost estimates for Grand Gulf 1 and Waterford 3. If the judge's separate allocation for Grand Gulf is upheld, the remedy should be the same for Waterford 3.

(2) Occidental Chemical Corporation and Georgia Gulf Corporation state that if production cost equalization is not adopted, then they support either: (1) adoption of the 1982 System Agreement but with the ER82-616 Grand Gulf allocation, updated to reflect the current cost estimates for Grand Gulf 1 and Waterford 3 or (2) another fixed responsibility allocation (as opposed to the ER82-483 shifting allocation) for both Grand Gulf 1 and Waterford 3, in proportion to the companies' most recent responsibility ratios.

(3) The City of New Orleans supports any of the three production cost equalization proposals if applied to all generating units. If none of those is adopted, however, it supports the Grand Gulf

equalization in ER82-483 but excepts to the approval of the 1982 System Agreement. If full production cost equalization *is* ordered, CNO asserts that it should cover *all* production plants, not just Grand Gulf and Waterford 3, because to do otherwise would deny NOPSI access to any coal-fired generation.

Middle South Services, Inc.

MSS's major objection to the judge's decision is the finding that cost responsibility for Grand Gulf should be revised annually. Contrary to the judge's belief, states MSS, there are no foreseeable shifts in demand patterns among the companies. Therefore, Grand Gulf cost allocation should be permanent. MSS claims that an annual revision of cost responsibility would render rates less stable, and that a permanent allocation would facilitate long-term plans for construction and retirement of capacity by each company.

Commission Trial Staff

The Commission Trial Staff position is aligned with that of the Louisiana parties. Staff excepts to the judge's refusal to order production cost equalization and claims that the judge's finding as to the pattern of automony on the system is unsupported by the record. The judge, states Staff, relied only on limited testimony in making this finding, and ignored other evidence regarding the lack of autonomy on the system as well as evidence of AP&L's historical dependence on the system. Staff also objects to the judge's conclusion that production cost equalization would result in a substantial departure from past practice.

Staff further excepts to the judge's conclusion at pp. 65,149 and 65,170 that cost equalization would divest the States of their control over rate base. Staff points out that transmission costs are already equalized without any suggestion that this affects ownership, control, or State jurisdiction. Additionally, Staff disputes any finding that equalization would alter representations made to

State commissions. In support, Staff states that the APSC historically relied on the operation of the system as a whole, and notes that the judge already rejected the MPSC's detrimental reliance argument.

Staff claims that there is no record basis for the judge's finding that Grand Gulf is any different from other system units, or for his Grand Gulf allocation. As for the 1982 System Agreement, Staff contends that it fails to meet its own objective of equalizing any imbalance of costs on the system and is itself a substantial departure from the historic operation of the system which produced a rough equalization of costs among the companies. Staff supports production cost equalization as the record-supported method of achieving the objectives of the system as expressed in the System Agreements over the past 30 years.

C. Commission Jurisdiction

Several jurisdictional challenges have been made in both dockets regarding this Commission's authority to amend the UPSA and the System Agreement. There are three major arguments: (1) Grand Gulf is a *generating* facility and thus is not under our jurisdiction under Section 201(b) of the Federal Power Act; (2) the Commission has no jurisdiction to force a purchase or sale of power, and thus cannot allocate any Grand Gulf costs to AP&L; and (3) the *Mobile-Sierra* doctrine precludes modification of the UPSA or 1982 System Agreement. We affirm the rejection of these arguments by Judges Liebman and Head (26 FERC at pp. 65,113-18; 30 FERC at pp. 65,146-47, 65,140-51, and 65,154), and find it necessary to add only briefly to their discussions.

First, we wish to address a recent Supreme Court case, *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission,* 461 U.S. 375 (1983), cited by the APSC, Arkansas Industries, the MPSC and MAG, and AMAX as supporting broader State jurisdiction over electric rates. In that case the

Court upheld the APSC's assertion of jurisdiction over a rural electric power cooperative under the supervision of the Rural Electrification Administration (REA). However, that case was quite different from the present one since it involved jurisdiction over rural electric cooperatives, which the Commission's predecessor (and a court of appeals) had determined were *not* jurisdictional under the Federal Power Act.[8] Finding no Federal preemption of State regulation of rural electric cooperatives under the Federal Power Act or otherwise, the Court next looked to whether the Commerce Clause limited State regulation and applied a balance-of-interests test in making its determination.

In the present case, there is clear Federal preemption since the sales for resale in interstate commerce among the Middle South pool members are now and have been subject to this Commission's and its predecessor's jurisdiction under the Federal Power Act. The Court in *Arkansas Electric, supra,* rejected the "bright line" distinction between wholesale and retail rates under the Commerce Clause, which had been enunciated in *Public Utilities Commission of Rhode Island v. Attleboro,* 273 U.S. 83 (1927). However, the Court emphasized that the "bright line" drawn by the Congress was still intact under the Supremacy Clause:

> *Southern California Edison Co.* and other cases have made it clear that the Federal Power Act draws a bright line between the respective jurisdictions of federal and state regulatory agencies. 461 U.S. at 392-3.

Where, as here, the Federal Power Act clearly provides for preemptive Commission jurisdiction over wholesale electric rates in

[8]The Court noted that if the Commission or courts were to ever determine that the Commission *did* have jurisdiction under the FPA over rural electric cooperatives, "we would obviously be faced with a very different preemption question." 461 U.S. at 383, note 7.

interstate commerce, the Commerce Clause question and the balance-of-interests test[9] under it are never reached.[10]

Next, in response to the argument that any change in Grand Gulf entitlements would constitute a forced purchase or sale, we find that the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent. In other words, the real issue is whether rates among those companies are just, reasonable, and not unduly discriminatory.

The Commission followed a similar line of reasoning in *Nantahala Power Co.,* Opinion Nos. 139 and 139-A, 19 FERC ¶ 61,152 (1982) and 20 FERC ¶ 61,430 (1982). In *Nantahala,* the Commission re-allocated energy entitlements between subsidiaries of an industrial company (Alcoa), in order to achieve just and reasonable rates. The two subsidiaries, Nantahala and Tapoco, had allocated certain TVA entitlements between themselves pursuant to 1971 Apportionment Agreement which revised the entitlements allocation under an earlier agreement. The Commission was careful to state that it was not reforming the 1971 Agreement and was not concerned with the mechanics of how entitlements were allocated; rather, it was setting *rates* as though Nantahala was receiving a fair share of entitlements. In upholding the Commission's decision, the Fourth Circuit stated that the Commission's burden in such a situation is not only to scrutinize rates, but also the fairness of all transactions allocating resources between subsidiaries. *Nantahala Power & Light Co. v. F.E.R.C.,*

[9]We read Judge Head's decision in Docket No. ER82-483, 30 FERC at pp. 65, 150-51, as completely consistent with this view on the jurisdictional question. His discussion of the need to balance Federal and State interests relates to policy concerns regarding the impact of Commission orders on retail rates, rather than to legal, jurisdictional concerns.

[10]In any event, it would be hard to imagine how, under a balance-of-interests test, one could characterize a multi-state pool agreement as a matter of primarily "local interest" with "only incidental" effects on interstate commerce.

727 F.2d 1342, 1348 (4th Cir. 1984). Although *Nantahala* is not directly on point, we believe that it provides support for the Commission's authority to set rates as though a different allocation existed.

Another matter related to the forced purchase/sale argument concerns AP&L's involvement in Grand Gulf. While the forced purchase/sale argument applies to all of the UPSA signatories, arguably it has more force in regard to AP&L since under the UPSA, AP&L has not agreed to buy *any* Grand Gulf capacity. However, we reject any assertion or implication by any of the parties that AP&L has had no involvement in the Grand Gulf unit, or that the unit was planned only for the other operating companies. As detailed in Judge Liebman's decision, 26 FERC at pp. 65,102-03, AP&L has been continuously involved in the system decisions regarding Grand Gulf and MSE. Of particular relevance is the fact that AP&L remains financially obligated to creditors for 17.1 percent of Grand Gulf project costs should the other operating companies not meet their obligations. (ER82-616, Ex. 1, pp. 7-15; Ex. 83; Tr. 353-8). We therefore find that AP&L cannot divorce itself from this case simply because the UPSA, as filed, allocates no Grand Gulf entitlements to it.

Lastly, concerning the jurisdictional argument that the *Mobile-Sierra* doctrine precludes the Commission from modifying the *voluntary* UPSA or 1982 System Agreement, we affirm and adopt the judges' rejections of this argument. (26 FERC at pp. 65,114-15 and 30 FERC at pp. 65,146-47.)

D. Federal/State Relationship

Several Arkansas parties argue that production cost equalization would impinge on State regulatory jurisdiction. Most of these arguments are appropriately considered by Judge Head, 30 FERC at pp. 65,148-51, and we find no need to add to his discussion except for the matters discussed below.

Several parties rely on the Supreme Court's recent recognition that "the States retain their traditional responsibility in the field

of regulating electric utilities for determining questions of need, reliability, cost, and other related state concerns." *Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Comm'n,* 461 U.S. 190, 205 (1983). However, they ignore the fact that the Court also expressly recognized this Commission's authority as an exception to that of the States:

> With the exception of the broad authority of the . . . Federal Energy Regulatory Commission, over the need for and pricing of electrical power transmitted in interstate commerce, . . . these economic aspects of electrical generation have been regulated for many years and in great detail by the states. 350 U.S. at 205-206.

Thus, we reject any argument that the Commission's authority over interstate sales was found subordinate to State jurisdiction in the *Pacific Gas* case.

In reference to the claim that production cost equalization would violate the doctrine of equitable estoppel insofar as the State commissions relied on certain representations made in State certification proceedings as to how costs would be allocated or how generating units would be used, Judge Head properly disposed of this issue in finding that a State commission could not reasonably rely on representations in State proceedings as guarantees against modification of the System Agreement, since this Commission alone has jurisdiction over the Agreement. (30 FERC at p. 65, 166.) Furthermore, the doctrine cannot operate to bind this Commission since we made no representations in and were not a party to any of the State certification proceedings.

E. Conflict with PURPA, PUHCA, or FPA

Some parties have argued that production cost equalization would conflict with the Public Utility Regulatory Policies Act (PURPA), 16 U.S.C. § 824a-1(b) (Supp. V 1981), the Public Utility Holding Company Act (PUHCA), 15 U.S.C. § 79, *et seq.*, and Section 202(a) of the Federal Power Act (FPA), 16 U.S.C. § 824a-1. They contend that Section 202(a) of the FPA

and Section 206(b) of PURPA are intended to encourage *voluntary* coordination and pooling arrangements among electric utilities, and that production cost equalization would have a chilling effect on coordination and conflict with this policy. It is also argued that production cost equalization would conflict with the SEC's jurisdiction over regulated public utility holding companies under PUHCA, since a principal purpose of PUHCA is to prevent manipulation of an operating utility owned by a holding company to the detriment of the customers of the operating utility.

Judge Head adequately rejected these arguments in his decision, 30 FERC at pp. 65,151-54, and we affirm and adopt his discussion.

F. Integrated Nature of the MSU System

Both Judge Liebman in Docket No. ER82-616 and Judge Head in Docket No. ER82-483 concluded that the records in their respective dockets supported a finding that the MSU system is integrated. (26 FERC at p. 65,106; 30 FERC at p. 65,167.) Judge Head, however, diverged from the reasoning of Judge Liebman by concluding that although the Middle South companies constitute a highly integrated electric system, the evidence also reveals a "pattern of autonomy," particularly as to decisions regarding specific plant site locations, fuel, and financing of new units. (30 FERC at p. 65,168.) He further determined that Grand Gulf was an "anomaly" to the regular planning and construction of units on the MSU system and, unlike other units, was intended to serve not just MP&L but rather the entire MSU system. (30 FERC at pp. 65,170-72.)

Having reviewed the evidence in both dockets, we affirm and adopt the findings of both judges that the Middle South companies constitute a highly coordinated integrated electric system. We conclude that this coordination and integration results in planning, construction, and operations which are conducted primarily for the system as a whole. We reject Judge Head's separate

findings that there is a "pattern of autonomy" on the system and that Grand Gulf is an "anomaly" to the regular planning and construction of system units.

The operation of the Middle System and the common officers and directors among MSU and its subsidiaries are described in detail by Judge Head at 30 FERC at pp. 63,141-43. Because of the overlapping officers and directors, and particularly because the System Operating Committee consists of representatives from each of the four operating companies and MSS, it is clear that there is input from the individual companies and consideration of their needs in making coordinated decisions. However, the evidence also is clear that major critical decisions, including decisions to build new generating units, are made by the Operating Committee for the benefit of the system as a whole. Our findings are discussed below. First, we review some basic pertinent provisions of the coordination agreements, followed by an analysis of the record evidence.

Section 3.01 of the "Objectives" sections of the 1973 and 1982 System Agreements[11] describes the basic purpose of the coordination among the companies. This section is almost identical in wording in the 1973 and 1982 versions. The 1982 version reads:

> 3.01 The purpose of this Agreement is to provide the contractual basis for the continued planning, construction, and operation of the electric generation, transmission and other facilities of the Companies in such a manner as to achieve economies consistent with the highest practicable reliability of service, subject to financial considerations, reasonable utilization of natural resources and minimization of the effect on the environment. This Agreement also provides a basis for equalizing among the Companies any imbalance of costs associated with the construction, ownership and operation of such facilities as are used for the mutual benefit of all the Companies.

[11] MSS Ex. 2 (1982 System Agreement); APSC Ex. 25 (1973 System Agreement).

Section 3.02 of the 1973 Agreement recognizes that economies of scale require planning, construction, and operation of bulk power supply "on the basis of a single system," and that this will dictate installation of generating units of the larger ratings available at that time, in generating stations of large size, strategically located with regard to fuel and water supply. The same section in the 1982 Agreement is shortened. It recognizes that economies of scale and integrated operations require that planning, construction, and operation of bulk power supply be "on a coordinated basis."

The System Operating Committee is the organization which historically has administered the provisions of the System Agreements among the four operating companies.[12] As stated above, it consists of representatives from each of the operating companies and MSS. Section 2.06 of the 1973 and 1982 Agreements provides that each company is to periodically furnish estimates of peak load and capability to the Operating Committee, and the Committee is to then determine a generation addition plan to provide capacity for the projected system load. Section 4.01 of the 1973 System Agreement requires that each company to whom the Committee "assigns" a generating unit for installation make the necessary financial arrangements and promptly proceed with the design and construction of the unit to meet the agreed upon "in service" date in the system plan. The 1982 System Agreement has the same requirement in Section 4.01, but does not use the word "assigns." Section 5.04 of the 1973 System Agreement provides that all decisions of the Operating Committee be by a two-thirds majority vote. Section 5.04 of the 1982 System Agreement changes this to a simple majority vote.

Several witnesses in the two dockets testified as to the nature of coordinated operations and the role of the System Operating Committee in decisions to build additional generating capacity on

[12]*Id.;* APSC Ex. 3 (1951 System Agreement memorandum).

the MSU System. Mr. Lupberger, an officer of MSU, MSE, and MSS, testified in Docket No. ER82-616. He stated that the Middle South System basically "is operated as though it were one electrical system under one ownership, and in all candor, probably could not be separated or pulled apart without detrimental effects to the customer economically." (Tr. 347.)

When asked who makes decisions on whether to build a new generating facility on the system, Mr. Lupberger stated that the decision to build in essence is a system decision, requiring concurrence of the system as a whole, with the decision to be based on the ultimate costs and perceived needs of the system as a whole for electricity, and the expected need for power of the company proposing to build the plant. (Tr. 348-49.) Mr. Lupberger noted that the individual companies make recommendations to the Operating Committee which, in turn, makes recommendations to the management of all the companies concerning the appropriate generation addition plan. (Tr. 395-96.) In his view, new units are not "assigned" or "dictated" by the Operating Committee, but rather are determined by the Committee's concurrence with the recommendations of the operating companies. (Tr. 397.)

Mr. Stampley, a senior vice president for MP&L and former System Operating Committee member, also testified in ER82-616, and generally agreed with Mr. Lupberger's description. He stated that over the last 10 to 15 years, the Operating Committee has been at the center of coming up with system recommendations, acting as a coordination point among the chief executive officers of the individual companies. According to Mr. Stampley, the Operating Committee makes recommendations as a committee, and the individual Committee members inform their chief executive officers that the recommendations come from the Committee as a group. These recommendations involve the general location, size, and type of plant to be built. (Tr. 739-42.)

Mr. Stampley further testified that past generation additions have been planned to serve the needs of the system and the companies that make up the system, with consideration given to such

factors as locational economies, achieving economies of scale, and achieving the most desirable proportion of reserves on the system. (Tr. 780-81.) According to Mr. Stampley, the Operating Committee was created to allow joint planning which in turn would allow the best service to the combined loads of all the companies and allow the best service to the public. (Tr. 782.) He stated that the decision that a particular company will be responsible for building a new unit is the result of a coordinated effort, and thus new units are "assigned" to be built only in the broadest sense. (Tr. 783-84.)

A third witness who testified in ER82-616, as well as in ER82-483, is Mr. Trumps, the director of the System Planning and Forecasting Department at MSS. Mr. Trumps agreed in ER82-616 that in the past generation planning has been done on a systemwide basis, but with due consideration of the needs of the individual companies as to the location of new facilities. (Tr. 911). He testified that the Operating Committee is responsible for developing generation addition plans from an engineering and operating standpoint, including recommendations as to the proper timing, location and types of units. (Tr. 912.) The Committee, he stated, was created to achieve the System's goal of achieving the best service to the system, the individual companies, and the public. (Tr. 914-916.)

In ER82-483, Mr. Trumps testified that a function of the Operating Committee is to make general decisions as to the size, location, and timing of units. The specifics as to size and location, he stated, are a function of the individual companies. (Tr. 2505-10.) He described the coordination process as one in which the individual companies participate in the development of the Operating Committee's consolidated power plans. These plans are submitted to and approved by the chief executive officers of the operating companies, and the boards of directors of the individual companies approve their own construction projects and expenditures. (MSS Ex. 17 at 6-8.) Mr. Trumps testified that the MSU

System has for at least the past 30 years planned, sited, constructed, financed, and operated production plant to minimize the system costs. However, in his view the decisions made were not totally from a system viewpoint since the individual companies also did studies as to what kinds of units were most appropriate for them. (Tr. 2693.)

Another witness in ER82-483 was Mr. Phillips, a senior vice president of AP&L, who testified that the Middle South companies in the past have agreed: to coordinate planning, construction, and operation of bulk power supply facilities on the basis of a single system; to size generating stations to achieve economies of scale; to strategically locate generation with regard to water and fuel supply; to plan generation to produce the lowest total cost on a system basis, consistent with reliability; to coordinate the plans of the individual companies so as to develop generation additions on a system basis, such that the companies' combined loads can be served with less aggregate installed capacity; and to share in the benefits and pay a share of the costs of coordinated operations. (Tr. 1000-04.)

Mr. Copeland, a former staff member of the APSC, the Arkansas Attorney General's Office, and the Arkansas Department of Energy, testified in ER82-483 as follows:

> Certainly, the system, overall, seeks to construct plants in the most economical fashion possible to benefit the total needs of the system. The system is not in the process or in the business to install excess capacity, systemwide, to make off-system sales. The ultimate objective of the operating committee is to make sure that on a systemwide basis, the planning is optimal for the system. And that does not mean, however, that individual plants within the system might not be built and designed for the individual operating companies, as long as that is not disadvantageous to the system as a whole. (Tr. 6729.)

The record in ER82-483 further includes testimony by Mr. Leo, Vice President of Economic Research at MSS, given in

another pending Middle South case in Docket Nos. ER81-428 and EL81-12. Mr. Leo was a member and chairman of the committee that drafted the System Agreement. He stated that,

> [t]he units [capacity additions] are installed, under past practice, in response to the projected combined load forecasts of the individual companies. Therefore, the units are sized for the system need rather than for the needs of the company installing the units. Therefore, there are generally companies that have more capacity available than their responsibility under the System Agreement. (LPSC Ex. 86 at Tr. 124-25.)

In addition to the extensive testimony of the above witnesses, the record in ER82-483 contains various sets of minutes of the System Operating Committee from 1961 to 1980. (LPSC Exs. 19-70; OCC Exs. 3-45.) These minutes reveal that the individual companies have had considerable input in the final Committee recommendations, but that it was the Committee that made critical decisions based on the needs of the system as a whole. The minutes show that the Committee members reached conclusions, recommendations, and agreements on a variety of matters such as revised system load and capability forecasts, general geographic locations on the system where new generating units should be located, which companies should tentatively be "assigned" to build certain units, the general size of new units, and allocation of MSE's Grand Gulf capacity.

As previously indicated, Judge Head adopted the position of certain Arkansas parties that there is "autonomy" on the part of the individual operating companies. These parties primarily rely on the fact that Section 4.01 of the 1982 System Agreement requires that each company "own, or have available to it under contract, such generating capability and other facilities as are necessary to supply all of the requirements of its own customers." They argue that all companies fully participate in the consolidated power plan, that the individual companies ask to build new units rather than having units assigned to them, that all final critical decisions regarding generation additions are made by the individual companies and not the Operating Committee, and that the System operates so that the company building a unit shares the new plant only until it can be absorbed by that company's native load. While some of these contentions may be true, neither they nor the above testimony nor the Operating Committee minutes support a finding of autonomy.

As shown in the Operating Committee minutes, there is no doubt that the individual companies have had input in Committee decisions and recommendations, and have actively sought to build certain generation units based on the needs of their individual loads. For example: in 1967, the Operating Committee agreed to AP&L's proposal to build an 800 MW nuclear unit for 1973 (LPSC Ex. 29; OCC Ex. 7); in 1969, the Committee considered company reports regarding the installation of new units for 1975 and 1976, and approved company plans for installation of oil or gas-fired units by MP&L, LP&L and AP&L (LPSC Ex. 35; OCC Ex. 11); and in 1970, the Committee agreed that AP&L should issue a letter of intent for a 1976 load nuclear unit (OCC Ex. 11).

Although the Committee often has concurred in the recommendations and plans submitted by the individual companies, however, the Committee minutes also show that the Committee has not automatically approved individual company plans and that its recommendations have been made based on overall system needs. For example:

(1) 1966 Committee minutes indicate that General Electric and Westinghouse had been requested to submit proposals for a nuclear plant to be operated for the peak of 1971, but it was clearly stated that it was unknown where in the system such unit, if any, would be placed. The companies were notified that their proposals for the unit would be analyzed not only competitively

between them, but also from the standpoint of economics with other fuels. The planning committee was to have a report to the Operating Committee on the 1971 unit location. (LPSC Ex. 26; OCC Ex. 4.)

(2) In 1966, LP&L reported that it was investigating the feasibility of installing a unit with a capability of either 550 MW or 750 MW. The Committee indicated that any decision by Louisiana to build a unit larger than 550 MW should be reviewed by the Committee for final approval. (LPSC Ex. 27; OCC Ex 5.)

(3) In 1967, the Committee agreed that AP&L should install a 750 MW unit at Ninemile Point in 1971 because of the long-range economic benefits to the Middle South System, as determined by studies of alternate sizes and potential load demands. The Committee emphasized its prior agreement that additional capacity must be installed between the New Orleans area and the northern part of the System by 1971. (LPSC Ex. 29; OCC Ex. 7.)

(4) In 1970, the Committee considered a report analyzing various factors associated with adding an 1165 MW 1978 nuclear unit at different locations on the system. These factors included best siting, stress on the transmission system, which company was short or long, etc. The Committee also concluded that if the 1978 unit was located in the south, there would be two nuclear units in the south and two in the north, thereby distributing nuclear energy evenly across the system. (LPSC Ex. 37.)

(5) In 1970, the Committee recommended that because of the tight oil and gas supply situation and need to obtain fuel for 2250 MW of capacity under construction, and expiration of present fuel contracts in 1977, the system should plan for a 1977 peak load nuclear unit in the southern end of the system. (LPSC Ex. 36; OCC Ex. 13.)

(6) In 1976, the Committee directed both AP&L and MP&L to proceed with investigations as though both of them were going to build a 1985 coal-fired unit, even though the preliminary analysis

indicated that the unit should be built in Mississippi. The Committee was to later develop a final recommendation as to which company should build the unit. (LPSC Ex. 57; OCC Ex. 32.)

(7) In 1977, the Committee agreed that for forecast purposes, it would be assumed that MSE would own all base load units scheduled for commercial operation in 1987 and later. It recommended to the chief executive officers that all future base load units not yet assigned be assigned in such a manner as to maintain equitable sharing of MSE units (i.e., assign units to levelize capability responsibility deficits insofar as practicable). (LPSC Ex. 60.)

This sampling of Committee minutes supports a finding that decisions on the MSU System are made based on an overall *System* plan and primarily for the system as a whole.

The Arkansas parties argue that new generation units were not assigned, but rather that individual companies volunteered for them. We believe the above evidence supports two major findings: (1) the operating companies were intimately involved in the planning stages of new generation units, sought to meet and promote the needs of their individual systems by "volunteering" to build particular units, and, once the Operating Committee "assigned" a unit to them, exercised their authority to decide details such as specific location, timing, and sizing of the unit; but (2) the Operating Committee nevertheless made the major decisions concerning general timing, location and size of plant additions, in view of the overall needs of the system, while accommodating individual company needs wherever possible. Whether units were "volunteered" for or "assigned" is not so relevent as the fact that operating companies ended up with responsibility for the units only where all the system companies, jointly acting as the System Operating Committee, concurred that this was in the best interests of the System as a whole.

As previously stated, Section 4.01 of the System Agreement makes each operating company responsible for owning or purchasing capability necessary to meet the requirements of its own customers. In our view, this requirement does not indicate autonomy insofar as final decisions to add generating facilities is concerned. While the companies may have an obligation to volunteer for new units recommended by the Operating Committee or may propose to build units to meet their native load, this does not negate the fact that the overall generation addition plan is reached by consensus of the Operating Committee, and that any proposed new units are approved by the Committee consistent with the overall system objectives.

Still another factor which refutes any contention that AP&L is an autonomous company which plans new units solely to meet its own needs is AP&L's dependence for over a decade on other operating companies to help meet the needs of its native load. This dependence is detailed in both initial decisions, and is amply supported by the records. 26 FERC at p. 65,100 and 30 FERC at p. 65,143.

We note that there appear to be no instances where an operating company has built a new unit without a recommendation to do so from the Operating Committee, or where a company has actually refused to build a unit once the Committee has recommended that it do so. Although some units have had to be cancelled or a company has had to back out of constructing a unit (for example, NOPSI found it was not feasible for it to construct Grand Gulf 2), these changes in system plans were made with the concurrence of the Operating Committee. (ER82-483 Tr. 4392-93; Tr. 1447-54.)

The "autonomy" argument must also be rejected in part based on the fact that the System Agreement itself removes considerable control from the individual companies. Mr. Trumps testified in ER82-483 that the 1982 System Agreement was changed to

provide for decisions by majority vote rather than a two-thirds vote to ensure that one company cannot block a Committee decision. Even under the 1973 Agreement, he agreed, a single company could be outvoted. (Tr. 2545-46.) Although he held the view that new units are not dictated or assigned by the Operating Committee, he stated that once a decision was made, an individual company could not veto that decision. (Tr. 84-85.)

G. The Grand Gulf "Anomaly"

We reject Judge Head's conclusion that Grand Gulf is an "anomaly" to the regular planning and construction of generating facilities on the MSU System. (30 FERC at p. 65,172.) We conclude that the above evidence and the history of generation additions on the System supports a finding that all generation additions, including Grand Gulf, have been planned in basically the same manner.

Both judges provide a good chronology of generation additions on the Middle South System, and their descriptions will not be repeated in detail here. (26 FERC at pp 65,100-02; 30 FERC at pp. 65,143-45.) Of primary importance in deciding the issues before us is the decision by the System in the late 1960's and early 1970's to change its fuel mix by shifting away from oil and gas generation and obtaining a greater proportion of nuclear and coal generation. Mr. Lupberger testified in ER82-616 that the national natural gas shortage in the 1960's, the loss of long-term gas contracts in Arkansas in the early 1970's and later at NOPSI, and the Arab oil problems and Federal government push to become less dependent on oil and gas, convinced MSU that fuel diversification was a necessary corporate strategy for building future base load capacity. (Tr. 369.) This strategy is now explicitly stated as a System objective in Section 3.03 of the 1982 System Agreement.

According to Mr. Lupberger, the first step in pursuing the new corporate strategy of fuel diversification was to build the nuclear unit ANO 1. (Tr. 370.) He stated that the decision to build the

unit was made on the part of AP&L and the system as a whole. (Id.; Tr. 462.) Mr. Stampley testified that AP&L was the first to install a nuclear unit because it had been a "short" company for at least a decade. (Tr. 823.) Mr. Trumps testified that considerations for installing both ANO 1 and ANO 2 in Arkansas included the facts that Louisiana, Mississippi, and NOPSI had previously installed and operated gas-fired units to serve the entire system, and that AP&L was the first company within the System to lose access to gas contracts. (Tr. 947-48.)

The Arkansas parties argue that the ANO nuclear units were planned and certificated based solely on the need to meet AP&L's load growth. While it may be true that AP&L needed the capacity from the ANO units,[13] and the APSC may have relied on this need in certificating the units, this does not negate the fact that AP&L's ownership of the units was the result of a joint decision by the System, as part of the overall System generation addition plan. Docket No. ER82-483 contains testimony to this effect by Mr. Phillips, Vice President and Chief Engineer of AP&L, submitted in the State proceedings (U-2286) on ANO 2 and in an environmental report to the Atomic Energy Commission (AEC) on ANO 1. In the ANO 2 State proceedings, Mr. Phillips stated that AP&L's generating capacity is jointly planned with the other Middle South companies and that, in addition to meeting AP&L's needs, the proposed ANO 2 would fit with the reserve requirements of the Middle South System. (APSC Ex. 6 at 23.) He also agreed that responsibility among the sister companies of MSU generally is planned for large facility construction and is done on a rotating basis, and that ANO 2 would be AP&L's contribution for that particular period. (CNO Ex. 51 at pp. 57-62.)

The ANO 1 environmental report submitted by Mr. Phillips to the AEC stated that all generation is planned to meet the forecasted load of the Middle South System as a whole, and that

[13]AP&L was in a deficit position, as defined in the 1973 System Agreement, from mid-1973 until 1980, when ANO 2 became commercially operational. (ER82-616, Tr. 1995.)

each of the four operating companies constructs generating units to meet the additional requirements of the entire Middle South System. (Staff Ex. 29.) Mr. Ritchie, then president of AP&L, testified in the ANO 1 proceeding before the APSC, stating that the System Operating Committee had determined that it was most desirable to have an 800 MW unit at that time, and that it would not be possible to install an 800 MW unit on the AP&L system if it were not for the interconnected and integrated operation of AP&L with the other MSU companies and interconnections with surrounding utilities in the area. (APSC Ex. 27 at pp. 8-10.)

The above evidence supports a finding that although AP&L alone may have been able to absorb all the capacity of the ANO 1 and ANO 2 units in a very short time,[14] the units nevertheless served not only the individual needs of AP&L, but also the need of meeting overall system load growth and the system goal of diversifying fuel mix.

In September 1970, LP&L announced plans to construct two other nuclear units on the MSU System, Waterford 3 and 4, and in December 1970, filed with the AEC for a construction permit for the units. (ER82-483 Staff Ex. 29.) In its environmental report submitted to the AEC for these units (*id.*), LP&L noted that the combined load of the System needed the capacity Waterford 3 would provide, and further stated:

> It has been the practice in the Middle South Systems to allocate the new generating unit in any given year to the individual company which shows the greatest deficit in its load and capacity analysis with certain transmission and fuel economic constraints. For 1977 the applicant [LP&L] is the member having the greatest deficit between load and capacity and therefore was the [choice] within the group for installing this additional capacity.

[14]ANO 1 came on line in 1974 and never became a participation unit under the 1973 System Agreement because its total capacity was needed by AP&L. ANO 2 came on line in 1980 and was a participation unit for only two months, until absorbed by AP&L. (ER82-483 MSS EX. 24 at pp. 6-7.)

The AEC, in granting a construction permit for Waterford 3, gave great weight to the fact that the unit was needed to furnish power to consumers in the MSU service area.[15]

Also in September 1970, MP&L indicated that it was willing to install the next nuclear unit on the System. Soon thereafter, in February 1971, NOPSI informed the Operating Committee of its desire to build a nuclear unit. (ER82-483 Tr. 1528-29.) As indicated in the initial decisions, MP&L and NOPSI originally were each assigned to build a nuclear unit but because of several problems such as siting, responsibility for both units was given to MP&L. MP&L, however, determined that it would be unable to finance one nuclear unit, much less two, and MSE was then formed to own the two units. (26 FERC at pp. 65,101-02; 30 FERC at pp. 65,144-45.)

The evidence supports a finding that the Grand Gulf units were originally planned in the same manner as the other nuclear units, i.e., to meet MP&L's needs, to meet System needs, and to meet the System goal of diversifying fuel mix. Mr. Lupberger testified in ER82-616 that initially the driving force behind Grand Gulf 1 was to meet the future load requirements of the System operating companies and the need to move away from dependence on oil and gas. (Tr. 365-66.) Mr. Stampley concurred that the Grand Gulf units were built to meet both System and individual company load growth (in this case MP&L's), as had been true of every unit ever built on the System. (Tr. 746, 756, and 1043.) Mr. Phillips stated in ER82-483 that the Operating Committee decided to go forward with Grand Gulf 2 based on the combined load forecasts of all the companies, not just MP&L's. (ER82-483 Tr. 1547-48.)

The MP&L and MSE joint petition to the MPSC for a certificate of public convenience and necessity stated that the proposed Grand Gulf project would serve as a major source of

[15] *In re Louisiana Power & Light Co.*, 7 AEC 762 (1974).

base load capacity for MP&L and the entire MSS pooling arrangement. (ER82-616 Ex. 46 at p. 13; ER82-483 MPSC Ex. 12.) The MPSC order granting a certificate also stated that the Grand Gulf units would serve as a major source of base load capacity for both MP&L and the entire area served by the Middle South System. (ER82-616 Ex. 80, p. 16.)

There is no doubt that there are differences between Grand Gulf and other System units. These were aptly pointed out in MP&L's brief opposing exceptions in ER82-483, at p. 53:

(1) Every other generating unit on the System has been owned by an individual operating company. No operating company owns any part of Grand Gulf, which is owned separately by MSE.

(2) Every other unit on the System has been built, and is or will be operated, by the company that owns it. MP&L is the builder and operator of Grand Gulf, but only as the agent of MSE.

(3) Every other unit on the System has been financed by the company that owns it. Grand Gulf is being financed by MSE, but with credit support by *all* the operating companies.

(4) The AEC permits and licenses for other nuclear units on the System were applied for by and granted to a specific operating company. Licensing for Grand Gulf was sought by both MSE and MP&L as co-applicants.

These differences, however, arose solely from the fact that MP&L became unable to finance the Grand Gulf units on its own. They do not contradict the fact that Grand Gulf 1 and 2 were planned in the same manner as the other nuclear units on the System.

Mr. Lupberger testified in ER82-616 that the decision to create MSE was made by the Operating Committee, the respective boards of all operating companies, and the parent company. As

far as the basic decision to build those units, however, he said the same general process was applied for the Grand Gulf units as for ANO 1 and 2, the difference being that AP&L was capable of financing the ANO units whereas MP&L, NOPSI, or any other operating company was not financially capable of handling Grand Gulf by itself. This, he said, was due to the much lower costs of the ANO units. (Tr. 350-51.)

As pointed out by Judge Head at p. 65,144, the Operating Committee and the financial departments of the operating companies considered joint financing as an alternate to forming the generation subsidiary, MSE. (ER82-483 Tr. 1546-47, 1556.) Consideration was also given to having MSE own all base load capacity subsequent to certain specific units then under construction, which would have resulted in MSE owning basically all new base load capacity and equalization of base load costs. (Tr. 2595, 2701.) MSS Board minutes reveal that MSS also considered a variety of alternative arrangements for ownership of future System generation units, including formation of a generation subsidiary to own only nuclear plants. (See ER82-483 LPSC Ex. 11 (minutes of February 14, 1973)). Any implementation of these ideas was cut short because of financial restrictions placed on MSE by its creditors, prohibiting MSE from embarking on any other construction at least until after Grand Gulf 1 becomes operational. (ER82-483 Tr. 2701.)

Had MSE not been formed, or some other financing arrangement made, it appears that the Grand Gulf units could not have gone forward since none of the operating companies could have independently financed their construction. (ER82-483 Tr. 1545-54.) We conclude that MSE was merely a financing vehicle necessitated by the fact that the Middle South System would have been unable to carry out its generation addition plan without MSE or another financing arrangement. Moreover, there is no reason to believe that the System would not have taken similar steps for any of the other units had the same financial problems prevailed. We therefore conclude that Grand Gulf is not an "anomaly" on the MSU System.

H. Resolution

Our discussion in the preceding section focused on the nuclear plants added to the Middle South System. There are several reasons for this:

(1) The System embarked on a program to carry out a corporate policy, now explicitly stated in Section 3.03 of the 1982 System Agreement, of moving toward a new fuel base of nuclear and coal generation.

(2) The System, along with the nuclear industry nationwide, has been confronted with an unexpectedly dramatic increase in costs, uncertainties and delays in the construction of nuclear plants such as Grand Gulf and Waterford 3. These same problems have not arisen with coal units. (ER82-616 Tr. 800, 843-5, 339-41.)

(3) As recognized by Judges Head and Liebman, MSU System generation costs were roughly equalized among the operating companies under prior coordination agreements, and it is the large cost escalations of Grand Gulf and Waterford that have disrupted this pattern. (Compounding the problem of dramatic cost escalations is the fact that the System overestimated its needs and will have an overabundance of reserves for years to come.) (26 FERC at pp. 65,100-03; 30 FERC at pp. 65,143-46 and pp. 65,168-69.)

(4) A factor differentiating nuclear plants from other plants on the System is location. Historically, a major consideration in determining plant location on the MSU System was access to ready fuel supply. (ER82-483 Tr. 912-13.) This is evidenced by the fact, noted by the judges, that in the 1960's and 1970's, System generation was located mainly in Louisiana and Mississippi to take advantage of available fuel supply, particularly low-cost natural gas in Louisiana. Such ready fuel access is not an important factor in locating nuclear plants. (*Id.*)

The evidence cited in the preceding section reveals an aggressive attempt by the MSU System to change its fuel base, particularly by adding nuclear generation. It further shows that each operating company was initially assigned at least one nuclear unit. In view of the unforeseen problems unique to constructing nuclear units,[36] and the fact that all Middle South System nuclear units have been planned to meet overall System needs and objectives, we conclude that some form of equalization of nuclear plant costs is necessary to achieve just, reasonable, and non-discriminatory rates among the MSU operating companies.[37]

The question before us is whether the 1982 System Agreement and the UPSA, as filed, together will achieve proper cost allocation. We conclude that they will not, but that the 1982 System Agreement in conjunction with Judge Liebman's allocation of nuclear capacity will achieve just and reasonable results. We affirm and adopt Judge Liebman's findings and conclusion that the proposal of the LPSC and OCC is the most equitable allocation proposal in the ER82-616 record, and that the Grand Gulf allocation therein will result in an equitable sharing of responsibility for all the nuclear capacity on the MSU System. Judge Liebman provides a sound basis for his conclusion and a thorough analysis of the other allocation proposals at pp. 65,109-13 of his initial decision, and his discussion will not be repeated here.

[36]The System Operating Committee recognized the problems unique to nuclear units in 1979 in discussing a 1990 nuclear unit assigned to LP&L. It agreed that because no one company could commit to the uncertainties of nuclear generation under the existing unreasonable lead time, regulatory problems, and financial difficulties, a system study should be done, with the cost of the study to be shared by all the operating companies, and that LP&L should not commit for the unit without further Committee authorization. (ER82-483 Ex. 64.)

[37]We note that major nuclear plant construction problems arose after the ANO units, which basically were pre-Three Mile Island regulations and prior to the major cost escalations and delays experienced by the nuclear industry in general. (ER82-616 Tr. 2199-2200.) However, based on our previous finding that the ANO units were part of the *System* plan to embark on a program to move away from oil and gas base load generation, we conclude that the costs of all nuclear units, including the ANO units, should be equalized in an equitable manner.

The LPSC and OCC proposal adopted by Judge Liebman, contained in Exhibit 124, determines Grand Gulf 1 allotments in a manner designed to equitably apportion throughout the pool the total nuclear investment costs of the Middle South System. Exhibit 124 derives the total investment provided by AP&L's ANO 1 and 2, LP&L's Waterford 3, and MSE's Grand Gulf 1 nuclear units (as of the date of record). Based on the respective 1982 average demand to average system demand ratio for each pool member, the exhibit determines each member's total average nuclear investment responsibility. Each member's nuclear investment responsibility is then compared to its owned nuclear investment. The shortfall between a member's owned nuclear investment and the proportionate assignment of average nuclear investment to that member represents the amount of Grand Gulf 1 investment to be allotted to that member. This investment differential is converted into MW's of Grand Gulf capacity and, ultimately, into Grand Gulf percentage entitlements.

The Grand Gulf allocation percentages derived in Exhibit 124, and adopted herein, are as follows:

AP&L	36%
LP&L	14%
MP&L	33%
NOPSI	17%
	100%

As indicated by Judge Liebman, this allocation will result in each company sharing the cost of nuclear capacity roughly in proportion to each company's share of System demand.[38]

[38]As pointed out by Judge Liebman, this proposal's focus on nuclear capacity does not disregard other System base load capacity since it recognizes that while there are some differences in the costs of non-nuclear generation among the companies, these cost differences are relatively minor compared to the cost differences for nuclear generation. (26 FERC at p. 65,110.)

The impact of these Grand Gulf allotments (or any other Grand Gulf allotments) on reserve equalization under Service Schedule MSS-1 of the 1982 System Agreement will likely be a change in the shortness or longness of each member. For example, when Grand Gulf 1 becomes commercially operable, to the extent that the fixed Grand Gulf allotment ratio exceeds (or is exceeded by) the monthly 1982 System Agreement responsibility ratio for a given pool member, that member will become either more long (or short) or less long (or short) for pool reserve equalization purposes. The excess capacity of the long members will be equalized in accordance with the 1982 Agreement, i.e., to the extent a member having excess capacity cannot reach voluntary agreements to sell its excess capacity and energy under Service Schedule MSS-4 (Unit Power Purchase), its excess capacity will be equalized among the short members based on the costs of the long member's intermediate generating units under Service Schedule MSS-1 (Reserve Equalization). Any excess energy will be shared with the pool under Service Schedule MSS-3 (Exchange of Electric Energy Among the Companies).

We conclude that the above Grand Gulf allocation, coupled with the operation of the 1982 System Agreement, will result in just, reasonable, and non-discriminatory rates for the MSU operating companies. We affirm and adopt Judge Head's findings and conclusions rejecting the various allocation proposals in the ER82-483 record, and his approval of the 1982 System Agreement, except to the extent that he finds there is autonomy on the System or that the generating units are not planned and constructed for the System as a whole."

"Specifically, we agree with Judge Head's rejection of the MPSC proposal to reinstate the participation unit concept. As found by the judge at pp. 65,166-67 of the initial decision, the MPSC proposal would be inequitable and discriminatory because it would result in MP&L avoiding all responsibility for Grand Gulf for approximately 10 years,

(Footnote continued on the following page)

We next address the relationship between the stated objectives of the 1982 System Agreement and our decision herein. The Agreement lists several major objectives, including:

(1) the planning, construction and operation of bulk power supply on a coordinated basis;

(2) the equalization among the operating companies of any imbalance of costs associated with the construction, ownership and operation of such facilities as are used for the mutual benefit of all the companies;

(3) the need of the companies to move toward a new fuel base of coal and nuclear generation;

(4) the long-term goal that each company will have its proportionate share of base load generating units (coal and nuclear) available to serve its customers either by ownership or purchase; and

(5) the intention that each company will be willing and able to provide its portion of the major facilities determined to be necessary, and to share in the benefits and pay its share of the costs of coordinated operation as agreed upon.

We find these System goals to be reasonable and conclude that the allocation recommended by Judge Liebman is consistent with and will promote the System's major objectives. Most important-

(Footnote continued from previous page)

after which time it would enjoy the benefits of the project in the less expensive years. In the meantime, the short companies (LP&L and NOPSI) would pay approximately $3 billion of Grand Gulf's costs.

As to the production cost equalization proposals, we do not find it appropriate or necessary to adopt any of those proposals since they would be a substantial change from the way costs previously have been allocated on the MSU system, and since the allocation adopted herein will ameliorate the cost disparities among the operating companies.

We reject Judge Head's recommended Grand Gulf allocation as inconsistent with our conclusions that Grand Gulf is *not* an anomaly on the System, and that equalization of *all* nuclear costs is necessary to achieve just, reasonable, and non-discriminatory rates.

ly, the allocation adopted herein will equalize the imbalance of costs resulting from nuclear units planned and constructed by and for the System as a whole, and will promote the System goals of increasing the System's nuclear fuel base as well as each company's proportionate share of nuclear fuel base.

One final matter concerns the suggestion by some of the Louisiana parties, in briefs on and opposing exceptions in Docket No. ER82-483, that if Judge Liebman's Grand Gulf allocation is adopted, then updated cost estimates for the Grand Gulf and Waterford nuclear units should be used. Because cost estimates for these units have been continually changing and because the costs as well as demand projections in ER82-616 were reasonable when made and were subject to cross-examination, we find it appropriate to adopt Judge Liebman's recommendation without modification at this time.

II. ER82-616 Rate Issues

In addition to setting forth the purchasers' entitlements to the output of Grand Gulf, the UPSA also establishes the rates that each purchaser will pay to MSE. The parties have raised a number of issues concerning these rates, all of which were thoroughly addressed by Judge Liebman. We affirm the judge on all issues, except for rate of return (discussed in Section IV, *infra*), depreciation, annual amount of decommissioning expense, amortization of limited-term electric plant, and use of an income tax formula.*

*We summarily affirm the judge on his decision to: (1) defer the approval of rates for Grand Gulf Unit No. 2; (2) allow MSE to include $5 million in property taxes in its estimate of total decommissioning expense; (3) require MSE to use an external sinking fund for accumulating decommissioning amounts; and (4) exclude from the formula rate customer service and sales expenses.

In reference to the issue of whether MSE should be required to periodically re-file the formula rate, we agree with and adopt those portions of the initial decision in which the judge held that, for the reasons given

(Footnote continued on following page)

A. Depreciation

During the initial period of Grand Gulf's operation, MSE proposes to calculate depreciation by the units-of-production (UOP) depreciation method, a method which determines depreciation per kilowatt-hour. After the initial shakedown period for the plant, MSE proposes to use the equal life group (ELG) depreciation method, under which plant components are segregated on the basis of their expected service lives and the investment in each group is amortized over its assigned life. The UOP and ELG methods are described in detail in the initial decision, 26 FERC at pp. 65,132-33.

Trial Staff was the only participant to object to MSE's proposed depreciation methods. The judge rejected Staff's argument against using the UOP method for Grand Gulf 1 during its initial operation, but held that in no event should the method be used for more than five years. He also rejected Staff's arguments against using the ELG method.

On exceptions, Staff states that while it does not object to the use of the UOP method for limited periods of time, the method should be used only for six to twelve months. It gives five reasons: (1) straight-line depreciation, and not the UOP method, is the generally accepted depreciation method for electric utilities; (2) the judge apparently presumes that Grand Gulf may need a shakedown period of up to five years, but the shakedown should be effectively completed within 12 months after the unit goes into commercial operation; (3) straight-line depreciation is much simpler

(Footnote continued from previous page)

in *Middle South Services Inc.*, Opinion No. 124, 16 FERC ¶61,101 (1981), *aff'd sub nom. Louisiana Public Service Comm'n v. F.E.R.C.*, 688 F.2d 357 (5th Cir. 1982), *cert. denied*, 103 S.Ct. 1770 (1983), and *Southern Company Services*, 22 FERC ¶61,047 (1983), MSE need not re-file the formula periodically. (26 FERC at pp. 65,147-48.) However, we do not agree with, and do not adopt, those portions of the initial decision in which the judge suggested that such filings are necessary. (26 FERC at pp. 65,146-47.)

to implement because it involves making only one estimate (remaining plant life) whereas the UOP method involves making two estimates (remaining plant life and capacity factor at which the plant will operate); (4) a NARUC report criticizes the use of the UOP method; and (5) in Staff's view, the Commission has looked with disfavor on the type of intergenerational equity which MSE wants to achieve, i.e., to use the UOP method to reduce charges under the UPSA during the first several years of operation in order to reduce the impact of rate increases needed to compensate for the costs of Grand Gulf 1 power during that time.

We find that the judge's acceptance of the UOP depreciation method in conjunction with a cost of service tariff is acceptable in principle, if the method is used only for a limited time period. The judge himself recognized that the UOP method should be applied only for the initial shakedown period of Grand Gulf 1, but nevertheless approved its use for up to five years. Because a shakedown period normally is approximately 12 months, and the UOP method is not the depreciation method that has been generally accepted by this Commission, we find that the initial decision should be modified to allow the use of the UOP method for no longer than 12 months. However, MSE will not be precluded in a future proceeding from seeking to extend this time period should the shakedown period actually take longer than 12 months.

Staff also excepts to the judge's acceptance of the use of the ELG method of depreciation after the initial shakedown period. It argues that ELG rates have not been accepted by the Commission in any previously litigated electric rate case, and that MSE did not meet the requirements for using the ELG method. Specifically, Staff claims that MSE identified property only in broad five-year increments; that it did not identify the units that would be grouped together with the same service lives; and that because Grand Gulf 1 is a new nuclear unit, MSE does not have

good mortality data for judging how retirements of various plant components tend to be distributed by age, which is necessary for the ELG approach to be feasible.

While the ELG depreciation method may be technically possible to implement, we are concerned that it will inhibit our ability to effectively monitor MSE's depreciation expense, particularly because the method involves many different depreciation rates and different groups of equipment being retired at different times. We have not previously accepted this depreciation method in a litigated electric rate case, and decline to do so here. Accordingly, MSE is directed to begin using the conventional straight-line depreciation method at the end of the initial 12-month period during which it is allowed to use the UOP depreciation method.

B. Annual Amount of Decommissioning Expense

A utility operating a nuclear generating unit eventually will incur the cost of decommissioning the unit. Since this is a cost of providing service from the unit, a portion of the total cost is chargeable each year to the ratepayers. The judge rejected MSE's proposal that the annual amount for Unit No. 1 should be set at an artificially low level of $324,000 during the first few years of the unit's life and then be allowed to rise. Instead, he adopted Staff's proposal that the annual amount of decommissioning expense be the same each year. This amount, the judge held, would be $1,236,876.

On exceptions MSE raises two points. The first is that the judge erred in adopting Staff's proposal. MSE argues that its proposal is preferable because the annual amount of decommissioning expense initially should be set at a low level. We disagree. The costs of decommissioning Grand Gulf are costs that are incurred in providing service from it. The ratepayers who take that service are responsible for those costs, and the principles of cost-based ratemaking suggest that ratepayers who take service now bear the

same relative decommissioning burden as those who take service later.[21] Staff's proposal carries out this objective. MSE's does not. We therefore affirm the judge's adoption of Staff's proposal.

MSE's second point is that, notwithstanding the merits of the issue, the judge erred in calculating the annual amount of decommissioning expense. This is correct. The judge used 100% of the total cost of decommissioning Unit No. 1 in calculating the annual amount. MSE, however, owns only 90% of Unit No. 1 and is expected to pay only 90% of the total cost of decommissioning that unit. (Ex. 49, p. 2; Ex. 22, p. 13.) The annual amount of decommissioning expense to be included in MSE's rates should therefore be calculated using the latter amount. The annual expense so calculated is $1,113,188.[22]

C. Amortization of Limited-Term Electric Plant

The judge permitted the formula rate to provide for amounts recovered in Accounts 404-407 and Accounts 411.6 and 411.7, but also held that no amounts could be recorded in these accounts without prior approval by the Commission. (26 FERC at pp. 65,148-49.)

[21]These general principles are discussed in *Columbia Gulf Transmission Co.*, Opinion No. 173, 23 FERC ¶61,396, at pp. 61,850-51, *appeal docketed sub nom. City of Charlottesville v. F.E.R.C.* No. 83-2059 (D.C. Cir. filed Oct. 6, 1983); *Tax Normalization for Certain Items Reflecting Timing Differences in Recognition of Expenses or Revenues for Ratemaking and Income Tax Purposes*, Order No. 144, FERC Statutes and Regulations ¶30,254 (1981), *reh. denied*, Order No. 144-A, FERC *Statutes and Regulations* ¶30,340 (1982), *aff'd sub nom. Public Systems v. F.E.R.C.*, 709 F.2d 73 (D.C. Cir. 1983).

[22]We note that although MSE's decommissioning cost estimates may be reasonable at this time, the company may seek adjustments to those estimates as more updated cost information is obtained. See *Commonwealth Edison Co.*, Opinion No. 165, 23 FERC ¶61,219 (1983), in which we held that Commonwealth Edison was not only free to seek, but was obligated to seek, adjustments to its depreciation rates as more updated depreciation information was obtained, in order to assure as near as possible full recovery of the costs of electric plants.

MSE excepts insofar as the judge required prior approval for amounts to be recorded in Account 404 (Amortization of Limited-Term Electric Plant). It claims that this is not consistent with the Uniform System of Accounts. The Uniform System of Accounts requires Commission approval before recording amounts in Accounts 405-417 and Accounts 411.6 and 411.7. It does not, however, require utilities to obtain our approval before recording amounts in Account 404.

No party has given any basis to be concerned that MSE would not use Account 404 properly. We therefore modify the initial decision such that MSE will not be required to obtain prior Commission approval for amounts included in Account 404.

D. Income Tax Formula

No party in this docket disputed MSE's use of tax normalization in determining its cost of service rates. Staff, however, suggested that a modified version of MSE's sample calculation of income tax expense be incorporated in MSE's proposed billing format, thereby becoming a formulary tax component of the UPSA.

The judge rejected this suggestion, finding that "Staff has offered no reason to support the inclusion of a tax formula, nor has Staff provided any support for the use of the sample calculation of income tax as a surrogate for an algebraic formula." (26 FERC at p. 65,143.) He noted that Staff had not cited any other unit power sales agreement on file with the Commission in which income taxes were represented in the rates by an algebraic formula such as that suggested by Staff. (*Id.*) Because MSE's sample calculation reflected uncertainty as to whether operations of Grand Gulf 1 would be subject to Mississippi income taxes, he further found that it would be inappropriate to attempt to fashion a tax formula to be included in the billing format prior to the time questions regarding the applicability of Mississippi income taxes are resolved. (*Id.*)

Staff excepts to the judge's ruling, claiming that it is important to set out a detailed calculation of both State and Federal income taxes in order to insure that MSE continues to compute income taxes incorporating tax normalization methods. Staff argues that MSE should be required to attach to its monthly billing statement to each operating company a step-by-step calculation of income tax expense as set out in Exhibit 72 (MSE's sample calculation of income taxes), since MSE will have to perform these calculations in any event and it would aid our accounting staff in verifying MSE's tax computation methods.

Although no party has argued that MSE will not properly normalize its income tax expense if a detailed formula is not included in the UPSA, we are concerned that we will not have an adequate opportunity to review the tax expense in MSE's rates unless some sort of sample tax calculation is provided to us. The Commission's general practice in recent years has been to require newly filed long-term unit power sales agreements to include a detailed tax computation as the tax component of the monthly billing statement.[23] This results in greater accountability of a utility in serving its unit power customers, and places no additional burden on the utility since it must make those detailed calculations in any event. Accordingly, we direct MSE to submit to us for approval a revised billing format, with an algebraic tax formula and an accounting treatment showing the detailed computation of the cost of service tax component.[24]

III. ER82-483 Rate Issues

In the proceeding concerning the 1982 System Agreement, Judge Head decided a procedural question (Tr. 1382-84) and six

[23] *See* South Carolina Generating Co., Inc., Rate Schedule FERC No. 1; AEP Generating Co., Rate Schedule FERC Nos. 1, 2, and 3.

[24] It has been argued that an algebraic formula is inappropriate because there is an unresolved question as to whether Grand Gulf 1 will be subject to Mississippi income taxes. To the extent that MSE is found not to be subject to Mississippi State income tax, this should be appropriately reflected in the rates.

miscellaneous rate issues (30 FERC ¶63,030, at pp. 65,131-39) to which exceptions have been filed. We affirm the initial decision with respect to four of the six miscellaneous issues.[25] We modify the initial decision with respect to Service Schedules MSS-3 and MSS-1, and we deny the exceptions to Judge Head's bench ruling in which he denied the admission of certain surrebuttal testimony, as discussed below. In this section we also affirm the judge on a further issue involving "time dating" of capital structure costs in Schedule MSS-4.

A. Service Schedule MSS-3 Adder

Service Schedule MSS-3 contains provisions governing the exchange and pricing of energy among the MSU operating companies. Energy is allocated on an hourly basis from the lowest cost sources, first to the loads of the companies owning the sources and second to the pool. The company that supplies energy to the pool is reimbursed for the current estimated cost of fuel, plus an adder determined by an algebraic formula in Section 30.08(f) of Service Schedule MSS-3. The MSS-3 adder is designed to reimburse the producing company for the incremental O&M costs associated with the production of additional energy.

The initial decision held that the MSS-3 adder was just and reasonable and that no strict cost support was required. The judge held that the operating companies should be allowed to recover

[25] We summarily affirm the initial decision with respect to its holdings that: (1) approval of the "cost of service" tariff represented by Service Schedules MSS-1 (Reserve Equalization), MSS-2 (Transmission Equalization), MSS-3 (Exchange of Electric Energy), and MSS-4 (Unit Power Purchase) will not be made subject to periodic review conditions; (2) the designation of transmission facilities (as Inter-Transmission Investment) in the cost equalization formula in Service Schedule MSS-2 is justified; (3) MSS's classification of intermediate generating units on the basis of fuel should be approved; and (4) MSS is justified in its allocation of administrative and general expenses to pool transactions and its use of labor ratios as the basis for doing so. (See 30 FERC ¶63,030, at pp. 65,131-37.)

their hard-to-quantify O&M costs through an adder. He found that the adder is analogous to the percentage adders allowed by section 35.23 of the Commission's regulations. Addressing CNO's concern that the adder provided for no cap, the judge stated that in *Ohio Edison Co.*, 23 FERC ¶ 61,344 (1983), the Commission approved the use of an uncapped 10% adder to recover hard-to-quantify, incremental O&M expenses without requiring strict cost support. (30 FERC ¶ 63,030, at p. 65,138.)

On exceptions, CNO repeats its claim that the adder lacks necessary cost justification. CNO contends that Order No. 84,[26] which established section 35.23 concerning percentage adders, is not applicable to the instant case, because no transmission arrangements are at issue here and the costs collected by the adder were not calculated as a percentage of purchased power costs as was contemplated in Order No. 84. CNO contends that the reasonableness of the 1 mill threshold endorsed by Order No. 84 does not prove the reasonableness of an adder for unquantifiable O&M expenses in this case. CNO further contends that the uncapped MSS-3 adder conceivably could exceed the level of reasonableness endorsed by Order No. 84. Finally, CNO claims that the MSS-3 adder may allow for the double recovery of costs, contending that O&M costs of intermediate generation are subject to collection through the reserve sharing provided in Service Schedule MSS-1. MSS opposes CNO's exceptions, following the rationale of the initial decision.

CNO's argument that section 35.23 is not directly applicable to the instant case has merit. In the preamble to section 35.23 in Order No. 84, the Commission noted that the "proposed rule was designed to limit percentage adders in all electric rates according

[26]Order No. 84, Limits for Percentage Adders in Electric Rates Transmission Service, Docket No. RM79-29, 45 Fed. Reg. 31,294 (1980) (reh. *denied* 12 FERC ¶ 61,017 (1980); further clarified in 12 FERC ¶ 61,157 (1980)). Order No. 84 also appears in FERC Statutes and Regulations, Regulations Preambles, 1977-1981 ¶ 30,153 (1980).

to whether a utility generated the electric power delivered or only transmitted it through an interconnection agreement." (FERC *Statutes and Regulations, Regulations Preambles,* 1977-1981 ¶ 30,153, at p. 31,031.) However, the notice and comment procedures yielded little cost data from which the Commission could have established a reasonable limit on generation adders, so the rulemaking focused on percentage adders that are used by utilities that perform transmission or purchase and resale functions in multiple party transactions. (Id.) The commission stated that it:

> continues to study the appropriateness of percentage adders when used for the primary generation of power and the interchange generation functions of transmitting utilities where the charge added to the overall charge for the power transmitted is based only on the internal incremental costs incurred by the transmitter.

(*Id.* at p. 31,035.) Thus, section 35.23, as established by Order No. 84, was intended to apply only to adders on third-party wheeling and multiple party purchase and resale transactions. MSS's transactions, in contrast, concern the sale of generation, and generation adders are not addressed by section 35.23. In view of this finding, *Ohio Edison*, cited by the initial decision as allowing uncapped percentage adders, does not apply to the instant case in the context of adders permitted by section 35.23. Further, in *Ohio Edison*, the uncapped adder served as a penalty to prevent abuse of emergency power service. 23 FERC ¶ 61,344, note 5 at p. 61,754. Such a rationale is absent here.

However, despite the foregoing, we nonetheless believe that the initial decision reached a correct result. MSS's cost plus a formula adder appears reasonable overall. First, the use of an adder is supportable here in principle, because adders are typically permitted for the recovery of difficult-to-quantify incremental costs. No party disputes that MSS's incremental O&M costs are difficult to quantify. Second, we believe that it would be inappro-

priate for MSS to use a percentage adder to recover such costs. Although a percentage adder is common industry practice in interchange transactions,[27] it would not serve the typical policy objectives in this case. In *Ohio Edison,* the Commission stated that in coordination transactions, an adder is allowed as an incentive to the selling utility to engage in such transactions. The Commission noted that, without some incentive above its incremental costs, a utility has no reason to undertake a coordination transaction and that such transactions usually reduce the cost of service to the buying utility and thus the ultimate consumer. (*Ohio Edison, supra,* at p. 61,749.) However, we believe that no such incentive structure exists between the affiliated Middle South companies, because the interchange transactions are wholly within the integrated System, are centrally dispatched, and are mandated by MSS rather than the individual companies. Thus, the operating companies do not require the incentive of a percentage adder in order to engage in these transactions.[28] Third, we believe that it is unnecessary for MSS to furnish specific cost support for the MSS-3 adder. Notwithstanding the fact that section 35.23 of our regulations governs another type of utility service, the section is nonetheless instructive in evaluating the present case. Section 35.23 reflects the general principle that, as an administrative convenience, we would not consider it cost-effective to require a utility to attempt to provide particularized support for difficult-to-quantify incremental costs as low as one mill per kWh.[29]

[27]*See* Ohio Edison Co., Initial Decision, 15 FERC ¶ 63,062, at p. 65,304 (1981), affirmed in part, and reversed in part in Ohio Edison Co., Opinion No. 170, 23 FERC ¶ 61,344 (1983); and Indiana & Michigan Electric Co., et al, 12 FERC ¶ 61,167, at p. 61,405 (1980).

[28]The issue of pricing in interchange transactions, among other things, is presently under review by the Commission. (See Notice of Inquiry, Docket No. RM85-17 (issued May 30, 1985).)

[29]See *FERC Statutes and Regulations, Regulations Preambles, 1977-1981, supra,* ¶ 30,153, at p. 31,034.

Under MSS's formula, it does not appear likely that the MSS-3 adder would exceed this one mill level.[30] Nor is the MSS-3 adder likely to produce as great a charge as would a ten percent adder. The MSS-3 adder appears to be MSS's attempt to determine its difficult-to-quantify incremental costs with some degree of accuracy. The charge produced using the adder is based on the ratio of current to base period incremental O&M costs as indexed in the formula. Thus, significant sudden increases in the adder appear unlikely. In contrast, an uncapped percentage adder would increase in proportion to the total costs on which it is based. Thus, with a percentage adder, it is possible that the amount recovered by the utility would increase at a more rapid rate that the unquantifiable costs which the charge is intended to collect.[31]

We reject CNO's allegation of possible double recovery of costs under the MSS-3 adder, because each of the MSS Service Schedules applies to different pooling functions. Thus, the *same* costs are not being recovered twice. Accordingly, we agree with the initial decision that the MSS-3 adder is justified and that no cost support need be filed at this time. However, if the MSS-3 adder should, at some future date, exceed a charge of one mill per kWh—or such charge as the Commission may ultimately rule to be determinative of whether cost support is required for generation adders in interchange sales, generally—then action may be taken at such time to require cost support for the adder. Therefore, we affirm the initial decision, as modified herein.

B. Service Schedule MSS-1 Adder

The MSS-1 adder gives credit to the operating companies, for reserve equalization purposes, for the value of capacity backed by

[30]For example, in order for the formula adder to exceed one mill per kWh, MSS's current incremental O&M costs would have to nearly double the O&M costs for the relatively recent base period.

[31]*See Ohio Edison Co.,* Initial Decision, 15 FERC ¶ 63,062, at p. 65,304 (1981).

reserves, which is purchased from non-affiliated utilities. The adder is calculated in accordance with an algebraic formula.

The initial decision approved the inclusion of the MSS-1 adder in the 1982 System Agreement. (30 FERC ¶ 63,030, at pp. 65,138-39.) On exceptions, CNO contends that the judge ignored the potential risk of disproportionately high credits to the purchasing utility under the sliding scale used in the adder and the fact that the adder treats sales of the same amount of energy differently. CNO questions the fact that the adder is affected by the amount of reserves on the Middle South System rather than those of the foreign seller which the adder is intended to reflect. CNO has also proposed subtraction of the amount of reserves that a Middle South company loses in a firm sale to a foreign utility, contending that MSS's failure to do so is discriminatory. Finally, CNO alleges that the adder provides an incentive to the operating companies to purchase firm power from outside the system despite "tremendous" reserves on the system.

We believe that the judge properly found that credit for the reserves associated with firm purchases is appropriate. Firm purchased capacity provides its own reserves and generally is more valuable than capacity not backed by reserves (such as unit power purchases). However, we also believe that CNO's alternative argument that the adder should reflect the *supplier's* reserves has merit. It appears more appropriate to fix the percentage credits for reserves so that they reflect the reserve level of the supplier; this avoids the possibility, using MSS's sliding scale reserve mechanism, that credit could exceed 100 percent of the capacity purchased. (*See* CNO Ex. 3, p. 36; Tr. 2089-91.) Therefore, we direct MSS to revise the MSS-1 adder to fix the percentage credits for reserves so that they reflect the reserve level of the supplier.

Regarding CNO's argument that there should be a subtraction of reserves for firm sales to foreign utilities, it appears correct, as argued by MSS and agreed to by Judge Head, that such a condi-

tion is unnecessary. MSS argued that firm sales would increase the selling company's Load Responsibility, thereby increasing its proportionate share of reserves, which would result in a reduction of the company's reserve equalization receipts and an increase in its payments. (MSS Reply Br., pp. 6-7; Initial Decision, 30 FERC ¶ 63,030, at p. 65,139.) Thus, there appears to be no undue benefit to an operating company making firm sales, and a penalty for such sales, as proposed by CNO, is unwarranted. Accordingly, we affirm the initial decision on the MSS-1 adder issue, as modified herein.

C. Capital Structure

Schedule MSS-4 permits MSU's operating companies to purchase capacity from a designated generating unit of another operating company. The judge accepted MSS's practice in Schedule MSS-4 of reflecting, in its monthly billing charge, the selling company's individual capital structure costs of embedded debt and preferred stock associated with the construction period of the designated generating unit from which the sale is made.

CNO excepts to the judge's adoption of the time dating practice, contending that the practice is not widely accepted and may result in undercollection or overcollection of revenues from various customer classes. In response, MSS argues that the practice of time dating is consistent with the narrowly defined purpose of Schedule MSS-4 to base charges on the costs of a contractually designated unit. MSS contends that the MSS-4 procedure represents a carry-over of the procedures used in MSS-1 of the 1973 System Agreement for participation units, and that the Commission granted implicit approval of that procedure in *Middle South Service, Inc.*, 16 FERC ¶ 61,101 (1981).

We agree with the judge that the practice in Schedule MSS-4 of basing charges on the capital costs of a designated generating unit is consistent with the Commission's ruling in the prior MSS

proceeding. Moreover, the use of this procedure for purposes of pricing individual unit power sales has previously been approved by the Commission.[32] Consequently, we affirm the judge's conclusion on this issue.

D. Surrebuttal Testimony

Surrebuttal testimony was filed by the Commission's Trial Staff, CNO, LPSC, and Occidental Chemical Company (OCC) in September 1983. Except for a portion of OCC's surrebuttal testimony, which was admitted on October 26, 1983 (Tr. 2375), all of the surrebuttal testimony was rejected by Judge Head in rulings from the bench during the evidentiary hearing session of October 11, 1983. (Tr. 1259-1384.)

OCC's surrebuttal, which consisted of 40 pages of testimony by Mr. Nathan, an economist, was intended to respond to contentions made in the rebuttal testimony of various witnesses representing MSS and several Arkansas interests. That testimony concerned the equity and efficiency of the cost equalization provisions. The judge denied admission of page 1 through most of page 31 of Mr. Nathan's testimony. (Tr. 1383.)

The judge based his decision on considerations of disruption to the administrative process and fairness to the other parties. (Tr. 1382-84.) Specifically, Judge Head found that OCC could have either filed testimony regarding the effect of MSS's proposal at an earlier date or, at least, moved earlier rather than waiting until the eve of trial to present such testimony. (Tr. 1382.)[33] Further, the judge noted that it would be unfair to the other parties to allow OCC to "wait until all of the other parties have had their say on what is a rather critical issue . . . and then have the opportunity

[32]*See, e.g., Connecticut Light and Power Co.*, Opinion No. 701, 52 FPC 175 (1974); *Public Service Co. of New Hampshire*, 20 FERC ¶ 63,015 (1982), *aff'd*, 22 FERC ¶ 61,229 (1983).

[33]The evidentiary hearing began on September 29, 1983.

to come in with the benefit of having everybody else's views on the table and express their opinion." (Tr. 1382.)[34] Addressing LPSC's motion, the judge also noted that surrebuttal testimony was not mentioned in the procedural schedule. (Tr. 1379.) Further, he stated that "there was ample time to have moved in advance to revise the procedural schedule if there was some perceived unfairness in connection with the way that testimony was filed back in July and August." (Tr. 1383.) The judge held that it was too late for OCC to seek to amend the procedural schedule to permit the filing of the surrebuttal testimony. (Tr. 1383.)

OCC did not seek to appeal the judge's evidentiary ruling to the Commission. However, on exceptions, OCC contends that the rebuttal testimony filed by MSS in August, 1983, was substantially more extensive than testimony originally submitted in support of the 1982 System Agreement as filed and that OCC's surrebuttal testimony was directly relevant to issues raised in MSS's rebuttal testimony. OCC maintains that admission of the surrebuttal testimony would not have delayed the ultimate resolution of this case and that the integrity of the procedural schedule should not *per se* have barred such important testimony from being submitted.

In a jointly filed brief opposing exceptions, the Arkansas and Missouri Public Service Commissions contend that if the surrebuttal testimony is admitted, then due process would require that the record be reopened in order to allow for written responses and cross-examination. The Arkansas and Missouri Congressional Delegations adopted the Arkansas and Missouri Commissions' brief. The State of Arkansas Office of the Attorney General also opposes OCC's exceptions.

Implicit in Judge Head's ruling is that he distinguished the excluded portion of OCC's surrebuttal testimony from the admitted portion based on his opinion that: (1) the admitted testimony was

[34]OCC did not file direct testimony.

not contained elsewhere in the record, and (2) there was "countering type testimony" on the part of certain of the Arkansas parties concerning a relevant issue in the case which the admitted surrebuttal addressed. (Tr. 1383, 2375-76.)

OCC has not demonstrated how the excluded portions of its surrebuttal may have changed the judge's analysis in the initial decision. Further, as the judge noted, the conclusive nature of the arguments made in OCC's surrebuttal testimony make them more appropriate for a brief than as expert testimony. (See Tr. 1353.) Finally, the admission of part of OCC's surrebuttal testimony indicates that the judge's desire to maintain the integrity of the procedural schedule did not serve as a *per se* bar to the surrebuttal testimony. We believe that Judge Head equitably balanced the interests of having a complete record (Tr. 1383-84), the interests of fairness to all parties, and the integrity of the administrative process (Tr. 1382-83), and we believe that he arrived at a sound ruling. Further, since no other parties who originally sought to introduce surrebuttal testimony have filed exceptions on this issue, we see no need to address OCC's additional request that those parties' surrebuttal testimony be admitted also. For the reasons stated, we deny OCC's exceptions to the judge's ruling on surrebuttal testimony.

IV. Rate of Return on Equity

We have before us a ratemaking scenario that is novel in several respects. First, we are evaluating two records and two sets of rates for MSU companies in tandem, and in each case MSU is used as a proxy for its subsidiaries in determining capital costs. Second, and even more significant, the older of the two evidentiary records (ER82-616) applies to rates that will take effect prospectively and well after the rates at issue in the other record (ER82-483). In essence, we are confronted with the same basic rate of return studies updated over a continuing period (i.e., the ER82-483 record updates the ER82-616 data.)

The same staff witness, Mr. Randall, presented rate of return recommendations in both dockets, based primarily on DCF analyses. The judge in each of the dockets accepted Mr. Randall's DCF analysis and adopted his recommendation, except that Judge Head in ER82-483 raised the staff recommendation based on certain changes occurring after the close of the record. (26 FERC at pp. 65,124-32; 30 FERC, at pp. 65,123-30). We affirm the rationale and conclusions of the judges in adopting Mr. Randall's methodology and rejecting the other record approaches as deficient.[35]

Having accepted Mr. Randall's methodology and assumptions, we must still determine what return on common equity is most representative for the periods during which the rates will be in effect.[36] Given the updated information that has been made available through the course of these proceedings and the fact that the rates in ER82-616 have not yet taken effect, we believe that the single rate of return adopted in this opinion on the basis of the cumulative information available in the records is appropriate for both dockets and both effective periods.

The hearing in ER82-616 began on March 14, 1983. Mr. Randall originally recommended a return on equity of 16.13% but, based on an updated DCF study, lowered his recommendation to 16.04% prior to the close of the record on May 12, 1983. The hearing in ER82-483 began on September 29, 1983. In that case, Mr. Randall originally recommended a return on equity of

[35]We do not agree, however, with Judge Liebman's conclusion that the range of reasonable returns in Docket No. ER82-616 is as limited as he determined, i.e., 15.9% to 16.2%. 26 FERC at pp. 65,131-32.

[36]For examples of cases in which the Commission has emphasized the need to determine a rate of return reflective of the period covered by the rates (and in doing so, evaluated post-record data), *see Illinois Power Co.*, 15 FERC ¶ 61,050 (1981); *Pacific Gas and Electric Co.*, Opinion No. 143, 20 FERC ¶ 61,190 (1982); *Minnesota Power and Light Co.*, Opinion No. 155, 21 FERC ¶ 61,233 (1982); and *Public Service Co. of New Mexico*, Opinion No. 164, 23 FERC ¶ 61,218 (1983).

15.86% but, based on an updated DCF study, lowered his recommendation to 15.35% prior to the close of the record on December 15, 1983. Thus, at the close of the record in ER82-483, which was some seven months after the close of the record in ER82-616, the most recent cost information supported a rate of return on equity of 15.35%.

Judge Head in ER82-483 determined that the record supported a range of returns of 15% to 16% for MSS's return on equity. While concluding that staff's rate of return analysis was the best reasoned and supported analysis in the record, he reassessed staff's 15.35% recommendation in light of two post-record events: a decrease in MSU's average stock price and recent news articles indicating an increase in the perception of risk for electric utilities with nuclear plant construction. He concluded that when these two factors are taken into account, the return on equity should be set closer to the high end of the zone of reasonableness. Accordingly, he set the return at 15.75%.

Several parties in ER82-483 excepted to Judge Head's use of post-record data to raise the rate of return.[37] We, too, have general concerns about adjusting a rate of return based solely on certain isolated changes that factor into a DCF analysis. Although falling stock prices may be indicative of increased capital costs, we are reluctant to raise a rate of return based on a change in only one element of the DCF analysis. Furthermore, if we were to adjust the staff's DCF analysis to reflect post-record changes in stock prices, presumably we would also, if requested, have to adjust the analysis to reflect post-record changes in dividend payouts and expected growth rates, the other elements of the analysis. The consequence of making the adjustment would thus be that the

[37]MSE argued that the same post-record data should be used to update Judge Liebman's recommended rate of return in ER82-616. We note, however, that to fully update that older record it is first necessary to consider the subsequent decreases in capital cost evidenced by the intervening ER82-483 record.

results of a DCF analysis could be continuously litigated. Although this course might make the allowed rate of return somewhat more reflective of current conditions, we question whether the gain in doing so would outweigh the "administrative necessity of closing the books at a time certain."[38]

In reference to the recent wave of highly publicized bad news for the nuclear power industry, the news articles relied on merely accentuate a fact already known and considered by the staff and the Commission for some time, i.e., that utilities building nuclear generating units generally face greater financial risk than other utilities. Additionally, we do not think it appropriate to modify a rate of return of a company based solely on news stories concerning other companies' nuclear construction problems.

Although we decline to adjust the record-supported rate of return based solely on news stories concerning the recent setbacks encountered in nuclear construction programs, or on the drop in MSU's stock prices, we note that since the close of both records, there has been a deterioration in the financial condition of MSU. Standard and Poor's Corporation recently downgraded several debt issue ratings of the MSU operating companies.[39] Moody's Investor Service, Inc., also downgraded MSE's $300 million in first mortgage bonds from Ba-1 to Ba-2, and assigned a Ba-2 rating to its new issue of $100 million in first mortgage bonds.[40] This downgrading is a significant and concrete factor specific to MSU and its subsidiaries, and presumably reflects perceptions of increased risk resulting from the construction of Grand Gulf 1 and 2, as well as any other changes in rate of return indicia specific to MSU and its subsidiaries. It is a factor that did not exist at the time of either initial decision. Thus, based on *all* of the above con-

[38]*Jersey Central Power & Light Co. v. F.E.R.C.*, No. 82-2004, slip op. at 11 (D.C. Cir., Mar. 30, 1984).

[39]*The Energy Daily*, Apr. 26, 1985, p. 4; *The Wall Street Journal* Apr. 26, 1985, p. 12.

[40]*The Wall Street Journal* May 16, 1985, p. 49.

siderations, particularly the recent downgradings, we believe that the allowed return should be somewhat higher than than recommended by Judge Head. We conclude that the rate of return in both dockets should be at the high end of the range of supportable returns established in ER82-483, since, as noted above, that docket contains an updated analysis of the methodology and data employed in ER82-616 (which rates have not yet gone into effect). We therefore adopt 16.00% as the appropriate allowed rate of return on equity for both dockets.

The Commission orders:[41]

Docket No. ER82-616-000

(A) The proposed settlement agreement filed in this docket and Docket No. ER82-483-000, on January 4, 1985, as revised on February 5, 1985, is rejected. Any motions filed in these dockets not acted on herein, or previously acted on, are denied.

(B) The initial decision issued in this docket on February 3, 1984, is affirmed to the extent not modified in this opinion.

(C) MSE shall revise the Grand Gulf Unit No. 1 entitlement percentages in Section 1.2 of the UPSA as follows:

AP&L 36%
LP&L 14%
MP&L 33%
NOPSI 17%

[41]Several miscellaneous matters are addressed in the ordering paragraphs below. We identify them here, although we do not believe that they require further explanation. Two issues presented in later dockets have been made subject to the outcome of Docket No. ER82-483 and should be treated in accordance with this opinion: (1) the MSS-1 O&M adder as applied in Docket No. ER83-66 (Letter order dated December 14, 1982); and (2) the return on equity to be applied in Docket No. ER84-283 (Letter order dated March 29, 1984). With respect to the UPSA at issue in ER82-616, a language change is being ordered so that Section 1.3 will properly refer to the Uniform System of Accounts for "Major" utilities rather than "Class A and B" utilities, consistent with our Order No. 390, *FERC Statutes and Regulations* ¶ 30,586, issued August 3, 1984.

(D) MSE shall remove from Section 1.2 of the UPSA the percentage allotments for Grand Gulf Unit No. 2, without prejudice to a subsequent filing.

(E) MSE shall delete Section 14 from the UPSA, which section provides that AP&L will have no rights or obligations under the UPSA.

(F) MSE shall amend Schedule B, Page 2, Cost Rate "C", and Section 1.3 of the UPSA to reflect the rate of return on equity adopted herein.

(G) MSE shall revise Section 1.3 of the UPSA to refer to the Uniform System of Accounts prescribed for "Major" utilities rather than "Class A and B" utilities.

(H) MSE may use the units of production depreciation method for one year. Conventional straight-line depreciation shall be used for the remainder of the service life of Grand Gulf Unit No. 1.

(I) The annual decommissioning amount allowed in rates shall be in accordance with this order, which is 90% of the amount approved by the judge, or $1,113,118.

(J) MSE shall file with the Commission an algebraic tax formula and an accounting treatment for tax items for derivation of income taxes.

(K) MSE may record appropriate entries in Account 404 (Amortization of Limited Term Electric Plant) without prior Commission approval.

(L) MSE shall file amendments to the UPSA to reflect the changes required in these ordering paragraphs, as well as any other amendments necessary to reflect the findings and conclusions in this opinion, within thirty (30) days of the date of this opinion.

Docket No. ER82-483-000

(M) The initial decision issued in this docket on February 4, 1985, is reversed as to the issue of Grand Gulf cost allocation. It is affirmed on all other issues, except as modified in this opinion.

(N) MSS shall amend the following 1982 System Agreement service schedules to reflect the rate of return on equity adopted herein:

MSS-1—Reserve Equalization—Section 10.06

MSS-2—Transmission Equalization—Section 20.06

MSS-4—Unit Power Sale—Section 40.05

(O) Service Schedule MSS-1, Section 10.02(c) shall be modified to provide a firm power purchase capacity credit based on suppliers' actual reserves rather than imputed reserves.

(P) MSE shall file amendments to the 1982 System Agreement to reflect the changes required in these ordering paragraphs, as well as any other amendments necessary to reflect the findings and conclusions in this opinion, within thirty (30) days of the date of this opinion.

(Q) Within thirty (30) days of the Commission's approval of the compliance filings ordered herein, the companies shall refund, with interest, any amounts collected in excess of those allowed pursuant to this opinion. Within fifteen (15) days thereafter, they shall file a report showing the computation of the refunds and interest paid. A copy of the refund report shall also be sent to all State regulatory agencies in States with customers affected by this order.

(R) Pursuant to a letter order dated December 14, 1982, the MSS-1 Operation and Maintenance Expense Adder modification in Docket No. ER83-66-000 is subject to the outcome of this docket.

(S) Pursuant to a letter order dated March 29, 1984, the Docket No. ER84-283-000 rate of return on equity modification from 18% to 16% is subject to the outcome of this docket.

(T) The motions for oral argument filed on March 26, 1985, by the LPSC, CNO, OCC and Georgia Gulf Corporation, and Jefferson Parish, Louisiana, are denied.

(U) The motion for a limited reopening of the record in Docket No. ER82-483, filed by OCC on April 4, 1985, is denied.[42]

(V) The motion to lodge an APSC order, filed by the LPSC, OCC and Georgia Gulf Corporation on May 28, 1985, is denied.[43]

Commissioner Richard's separate statement is attached.

---

[42]In support of its motion, OCC stated that Judge Head had relied only on the "first-hand, personal knowledge" of one witness in making his finding that there is autonomy on the part of the MSU operating companies. OCC sought to reopen the record to introduce other "first-hand, personal knowledge" contradicting that relied on by Judge Head. OCC's motion is moot given our finding herein that the record does not support Judge Head's autonomy finding.

[43]This motion sought to lodge an April 3, 1985 order of the APSC in an AP&L retail rate case. The movants sought to bring to the Commission's attention portions of the order in which the APSC discussed the relationship between MSS and MP&L, and in which the APSC recognized that the amount of AP&L White Bluff capacity purchased by LP&L and NOPSI was an offset to the Arkansas retail cost of service. This motion is now moot given our findings concerning the integrated nature of the MSU System and the interrelationship of the MSU subsidiaries.

Statement of Commissioner Oliver G. RICHARD III in Response to "Motion Requesting Recusal" in Docket Nos. ER82-483-000, Middle South Services, Inc.; and ER82-616-000, Middle South Energy, Inc.

Arkansas Power & Light Company (AP&L), the Attorney General of the State of Arkansas, the Attorney General of the State of Mississippi and the Cities of Conway and West Memphis, Arkansas have requested that I recuse myself from participation in the *Middle South* proceedings.[44] I find no merit in the motion, and decline to recuse myself.

The moving parties maintain that my past employment by Senator J. Bennett Johnston of Louisiana, who, along with the full Louisiana Congressional delegation, has intervened in Docket No. ER82-616, creates the appearance of bias which denies them a fair hearing. I disagree.

Between 1977 and 1981 I worked as a legislative assistant to Senator Johnston. In that capacity, I advised him on a wide variety of issues, including energy issues. I also assisted in drafting legislation that the Commission now implements. However, my employment with the Senator ended in August 1981, almost one year before the *Middle South* proceedings began. I had no prior contact with the facts or legal issues involved in *Middle South* before joining the Commission in 1982.

I fully agree that all parties to a Commission proceeding are entitled to a fair hearing before an impartial decisionmaker. There are no facts or circumstances arising from my prior employment or relationship with Senator Johnston that impair my impartiality. My employment with the Senator ended three years ago; I have had no prior contact with *Middle South;* and I have expressed no opinion about the merits of the proceedings.

[44]Responses in opposition to the motion have been filed by the Louisiana Public Service Commission; Louisiana Power & Light Company; New Orleans Public Service Company, Inc., the City of New Orleans, Louisiana and the Occidental Chemical Corporation.

Furthermore, contrary to the claim of the Cities of Conway and West Memphis, I have had no business association with "residents of Louisiana" since joining the Commission.[45]

The nature of Senator Johnston's involvement in *Middle South* further precludes an "appearance of impropriety" based on my relationship with him. He is participating as a public official pursuing policy goals rather than as a private individual with an economic stake in the outcome of these proceedings. As a formal intervenor before the Commission, the Senator, along with the entire Louisiana Congressional delegation, will place his opinions on the record, subject to rebuttal by any other party. Thus, contrary to AP&L's assertion, the Senator's intervention bears no resemblance to the sort of extra-record questioning of decisionmakers by Congressmen that has sometimes been held to impair the integrity of the decisionmaking process. My own decision in *Middle South* will be based solely on the evidence established in the record.

I have also considered the cost of recusal. Recusal is not a matter to be undertaken lightly. Just as a decisionmaker has a duty to recuse himself in the proper circumstances, he has a concomitant obligation not to recuse himself without a valid reason. *Simonson v. General Motors Corporation,* 425 F. Supp. 574 (D.C. Pa. 1976). This consideration is even truer for regulators than for

[45]The Cities contend that my "subsequent business association with residents of Louisiana whose interests are now contrary to those of the Arkansas parties in these cases create[s] an appearance of impropriety." I do not know what they mean. I have no financial ties to any "residents of Louisiana," including my former law firm of Hayes, Durio & Richard. My former firm is not involved in the *Middle South* proceedings. If the Cities are alleging that as ratepayers my former partners have interests adverse to the residents of Arkansas, then they have not raised grounds for recusal. Indeed, they're not even ratepayers. The possibility that a proceeding will affect the future utility bills of the decisionmaker *himself* as a member of the general public does not create a financial conflict of interest that warrants recusal. In Re Natural Gas Antitrust Litigation, 620 F.2d 794, 796-97 (10th Cir. 1980). In Re Virginia Electric and Power Co., 539 F.2d 357, 368 (4th Cir. 1976).

judges. A Commissioner who withdraws from a case cannot be replaced, as a judge can.[46] Since a Commissioner has a policymaking as well as a judicial role, his policy insights and outlook are lost to the collective decisionmaking process of the agency, if he fails to participate. I will give full and fair consideration to the merits of these proceedings, and, by any objective standard, there is no reasonable basis for concern about bias. Accordingly, I have an obligation to participate in these important matters, and thus deny the motions by the aforementioned parties.

[46]By way of analogy, Justice Rehnquist has pointed to the fact that Supreme Court Justices cannot be replaced as one reason they should be more reluctant than lower court judges to disqualify themselves. Laird v. Tatum, 409 U.S. 824 (1972), memorandum of Rehnquist, J.

APPENDIX F

FERC Opinion No. 234-A,
Middle South Energy, Inc.,
Docket Nos. ER82-616-000, ER82-616-005 through ER82-616-015, ER82-616-017 through ER82-616-024, and ER82-616-028;
Middle South Services, Inc.,
Docket Nos. ER82-483-000, ER82-483-003 through ER82-483-021, and ER82-483-024

Middle South Energy, Inc., Docket Nos. ER82-616-000, ER82-616-005 through ER82-616-015, ER82-616-017 through ER82-616-024, and ER82-616-028;

Middle South Services , Inc., Docket Nos. ER82-483-000, ER82-483-003 through ER82-483-021, and ER82-483-024

Opinion No. 234-A; Order Denying Rehearing and Granting Interventions

(Issued September 26, 1985)

Before Commissioners: Raymond J. O'Connor, Chairman; A.G. Sousa and Charles G. Stalon.

On June 13, 1985, the Commission issued Opinion No. 234, 31 FERC ¶ 61,305, involving the appropriate allocation of capacity costs incurred on the Middle South Utilities (MSU) System, including the cost of the Grand Gulf 1 nuclear unit, among the four wholly owned subsidiary operating companies of MSU. The four operating companies are Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (MP&L), Arkansas Power & Light Company (AP&L), and New Orleans Public Service, Inc. (NOPSI). Opinion No. 234 determined that all MSU System production costs should not be equalized among the operating companies, but that nuclear capacity investment costs should be equalized. To achieve this, the Opinion adopted the following Grand Gulf 1 allocation percentages which had been recommended by Judge Liebman in an initial decision issued in Docket No. ER82-616, 26 FERC ¶ 63,044 (1984): AP&L: 36%, LP&L: 14%, MP&L: 33%, NOPSI: 17%, Total: 100%.

Requests for rehearing of Opinion No. 234 were filed on July 3, 11, 12, and 15, 1985, by the following parties: Arkansas Industries; Mississippi Legal Services Coalition; Occidental Chemical Corporation and Georgia Gulf Corporation; the Attorney General of the State of Mississippi; the Louisiana Public Service Commission (LPSC); the Cities of Conway and West Memphis, Arkansas; the Arkansas Public Service Commission and Missouri Public Service Commission (APSC/MoPSC); MP&L; the Arkansas and Missouri Congressional Delegations; AP&L; Mississippi Representative Webb Franklin; AMAX, Inc; the Cities of Benton, North Little Rock, Osceola, and Prescott, Arkansas, and the Farmers Electric Cooperative Corporation; Jefferson Parish, Louisiana; the State of Arkansas (which joins in and adopts the rehearing request of the APSC/MoPSC); Middle South Energy, Inc. (MSE); LP&L and NOPSI; the Mississippi Public Service Commission (MPSC); the City of New Orleans; and Mississippi Industries. Eight of these parties also filed requests for a stay of Opinion No. 234, either pending rehearing or pending appellate review.

On August 2, 1985, the Commission issued an order granting rehearing for purposes of further consideration and denying a stay. 32 FERC ¶ 61,207. The portion of the order denying a stay was clarified and rehearing of the stay denial was denied by order issued September 3, 1985, 32 FERC ¶ 61,346. This order addresses the issues raised in the requests for rehearing of Opinion No. 234.

The arguments raised on rehearing concern the Commission's authority to reallocate Grand Gulf capacity costs, the line between State/Federal jurisdiction in this area, our findings concerning the integrated nature of the MSU System and decision-making on the System, and the appropriateness of the precise allocation plan we adopted. For the most part, the arguments raised on rehearing are ones that were already made and considered on exceptions. We have reviewed the arguments and conclude that rehearing should be denied. However, there appear to be certain areas of the Opinion which we need to clarify or expand upon, and certain mis-statements or erroneous interpretations of the Opinion made on rehearing which should be addressed. These are discussed below.

Commission Jurisdiction

On rehearing, numerous parties[1] again raise several arguments concerning the Commission's authority to amend the UPSA and

[1]AI; the APSC/MoPSC; the Cities of Conway, *et al;* the Arkansas and Missouri Congressional Delegations; the Cities of Benton, *et al.*, AP&L; AMAX, Inc.; and the MPSC.

the 1982 System Agreement. The major arguments, also raised previously below, are: (1) Grand Gulf is a generating facility and thus is not subject to our jurisdiction under Section 201(b) of the Federal Power Act (FPA); (2) MSE is not a "public utility" under Section 201(e) of the FPA, and thus is not subject to our jurisdiction; (3) the Commission has no jurisdiction to force a purchase or sale of Grand Gulf, and thus cannot alter the contractually agreed upon allocations; and (4) the *Mobile-Sierra* doctrine[2] precludes modification of the voluntary UPSA and 1982 System Agreement.

We rejected the above arguments in Opinion No. 234 primarily by summarily adopting the discussions of Judges Liebman and Head, 26 FERC at pp. 65,113-18 and 30 FERC at pp. 65,146-47, 65,148-51,[3] and 65,154. Some parties, for example the APSC/MoPSC, argue or imply on rehearing that the Commission failed to articulate its reasons for rejecting arguments that it lacks jurisdiction to order AP&L to purchase a portion of Grand Gulf capacity. We have again reviewed all of the jurisdiction arguments of the parties, as well as the portions of the judges' decisions which we affirmed. Although the initial decisions each focus on our authority to amend separate contracts, we believe that, taken together, they sufficiently address the majority of the challenges made to our jurisdiction in the two dockets, and we continue to agree with their general reasoning and conclusions. In view of certain matters raised on rehearing, however, we wish to expand briefly on the judges' discussions and to clarify our position concerning certain alleged inconsistencies between the judge's decisions. First, we think it appropriate to review the judges' discussions, cited above, concerning jurisdiction.

[2]*United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332 (1956) (*Mobile*); and *Federal Power Commission v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956) (*Sierra*).

[3]We wish to correct a typographical error at p. 61,643 of the Opinion which referred to pp. 65,140-51. This should be pp. 65,148-51.

In response to the Arkansas parties' arguments that the Commission lacks jurisdiction to allocate any Grand Gulf cost responsibility to AP&L, Judge Liebman initially found that AP&L had been extensively involved in every aspect of the decision to build, finance, and allocate the unit. He further found that Section 206(a) of the FPA clearly gives the Commission authority to supervise contracts among utilities and also mandates that the Commission revise the terms of such contracts to eliminate undue preferences or discrimination.[4] He concluded that the argument that there is no jurisdiction to adjust the UPSA percentages could not be reconciled with the Commission's duty under Section 206(a), and would also render meaningless the independent prohibition against undue discrimination embodied in Section 205(b) of the Act.

Judge Liebman next rejected the Arkansas parties' reliance on the *Mobile-Sierra* doctrine, *supra,* noting that in the *Mobile* Opinion, the Court was careful to emphasize that its holding in no way impaired the regulatory powers of the Commission, since the rate contracts in question remained "fully subject to the paramount power of the Commission to modify them when necessary in the public interest." 350 U.S. at 344. He also noted the Court's recognition in *Sierra* of the Commission's undoubted power under Section 206(a) to prescribe a change in contract rates whenever it determines such rates to be unlawful. He concluded that it was clear from the record that the failure to allocate any portion of Grand Gulf power and costs to AP&L confers an undue preference on AP&L without factual justification and unduly discriminates against the other operating companies. This failure, he

[4]Judge Liebman specifically noted that Section 206(a) of the FPA provides in pertinent part that if the Commission finds that any "*contract affecting*" any jurisdictional "rate, charges, or classification, demanded, observed, charged, or collected by any public utility" is "unjust,unreasonable, unduly discriminatory or preferential," the Commission is directed to "determine the just and reasonable . . . *contract to be thereafter observed and in force*, and shall fix the same by order." (Emphasis added.) 26 FERC at pp. 65,113-14.

stated, fits within the "unduly discriminatory" component of the *Sierra* test and thus "adversely affects the public interest."[5] Judge Liebman further found that the *Mobile-Sierra* doctrine does not abrogate but rather reinforces the FERC's power under Section 205(b).

Next, Judge Liebman distinguished *Municipalities of Groton v. F.E.R.C.*, 587 F.2d 1296 (D.C. Cir. 1978), and *Central Iowa Power Cooperative v. F.E.R.C.*, 606 F.2d 1156 (D.C. Cir. 1979), which had been relied upon for the proposition that voluntary contracts could not be revised. He further rejected the argument that *Southern Company Services, Inc.*, 20 FERC ¶ 61,332 (1982) and *Georgia Power Co.*, Opinion No. 711, 52 FPC 1343 (1974), precluded the Commission from ordering new entitlements.

Judge Liebman thus denied assertions that the Commission has no authority to modify the UPSA or compel AP&L to purchase Grand Gulf capacity, although he did not directly discuss Section 201 of the FPA.

Judge Head followed the general reasoning of Judge Liebman. His discussion of jurisdiction issues began with a rejection of the Arkansas parties' *Mobile-Sierra* arguments, particularly the contention that the doctrine allows abrogation of voluntary contracts only in cases of "unequivocal public necessity." He distinguished the *Mobile-Sierra* line of cases and, as did Judge Liebman, noted the *Mobile* Court's finding that contracts remain fully subject to the Commission's power to modify them in the public interest, as well as the *Sierra* holding that the Commission has power under

[5]The "unduly discriminatory" component of the *Sierra* test to which Judge Liebman referred is the Court's holding that the purpose of the power given the Commission by § 206(a) is the protection of the public interest, as distinguished from the private interest of utilities, and that: "[T]he sole concern of the Commission would seem to be whether the rate is so low as to adversely affect the public interest—as where it might impair the financial ability of the public utility to continue its service, cast upon other consumers an excessive burden, or be unduly discriminatory." 350 U.S. at 355.

Section 206(a) to prescribe a change in contract rates where such rates are determined to be unlawful. He further found that the *Mobile-Sierra* doctrine makes it clear that the Commission has power, pursuant to Sections 205 and 206 of the FPA, to revise the System Agreement on the basis that it is unjust, unreasonable, unduly discriminatory or preferential.

In reference to arguments that Sections 201(a) and (b) of the FPA prohibit cost equalization because it would extend Federal jurisdiction over generating plants and would intrude into state jurisdiction, Judge Head concluded that while the statutory language indicates that the Commission has jurisdiction only over matters not subject to state regulation, and does not have jurisdiction over generating facilities, nevertheless it specifically gives the Commission authority over the sale of electric energy at wholesale and, as a result, there is no doubt that the Commission has jurisdiction over the 1982 System Agreement. He further concluded that since the 1982 System Agreement constitutes a rate change filed under Section 205, the jurisdiction of the Commission under Section 206(a) to revise the agreement and set different rates cannot reasonably be challenged.

Next, Judge Head cited the Supreme Court's recent decision in *Arkansas Electric Corp. v. Arkansas Public Service Comm'n*, 461 U.S. 375 (1983), which he interpreted as broadening the area of state regulation but also as recognizing the need to reconcile and accommodate the competing demands of state and national interests. Judge Head stated that the Middle South case required such reconciliation and that while state commissions clearly have control over the generating plants they have approved for construction, nonetheless this Commission has authority under Sections 205 and 206 to assure that inter-company transactions are just, reasonable, nondiscriminatory and non-preferential. He concluded that the language in Section 201(a), restricting the FERC's authority to matters not subject to state regulation, does not nullify the Commission's clear authority to regulate the 1982

System Agreement, even if the exercise of FERC jurisdiction might appear inconsistent with the broadly expressed statement in Section 201(a). The fact that state commissions also have regulatory power in an affected area, rate base, does not preclude exercise of the Commission's authority, he concluded.

In light of the above findings, Judge Head held that production cost equalization was within the jurisdiction of the Commission if there were sufficient public interest reasons to revise the 1982 System Agreement in that fashion, but that the statutory scheme of the FPA and the deference that should be paid to state rate-making authority were factors to be considered as weighing against production cost equalization.

Judge Head thus followed Judge Liebman's general reasoning concerning Commission authority under Sections 205 and 206 to amend contracts. His focus, however, was on the System Agreement rather than on the UPSA or MSE.

Later in his discussion, Judge Head focused briefly on the specific question of whether equalization constitutes a forced purchase of capacity. He stated that while it is correct that the FERC cannot compel one utility to purchase from or sell to another (citing *Southern Company Services, Inc.*, 20 FERC ¶ 61,332 (1982)), this situation is not present in the instant case. He concluded that this proceeding is not dealing with a forced purchase, but rather with the proper method of allocating costs under the 1982 System Agreement.

As previously indicated, we interpret the above findings of the two judges to be generally consistent. However, because the judges were each focusing on different contractual agreements, we shall review the pertinent provisions of the FPA and clarify our position on any perceived inconsistencies between the two decisions.

Sections 201(a) and (b) of the FPA set forth the Commission's jurisdiction:

> Section 201.(a) It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this Part and the Part next following and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.
>
> (b)(1) The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and *to the sale of electric energy at wholesale in interstate commerce*, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, *but shall not have jurisdiction, except as specifically provided in this Part and the Part next following, over facilities used for the generation of electric energy* or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter. (emphasis supplied)

We agree with Judge Head that while the statutory language of Section 201 of the FPA grants the Commission jurisdiction only over matters not subject to state regulation, and explicitly removes from Commission jurisdiction facilities used for the generation of electric energy (except as specifically provided), it nevertheless explicitly grants jurisdiction over the sale of electric energy at wholesale in interstate commerce. It, therefore, is clear

that we have jurisdiction under Section 201 over the 1982 System Agreement because the agreement involves sales of electric energy at wholesale in interstate commerce. Despite the statutory language that the Commission does not have jurisdiction over generating facilities, we further conclude that Section 201 does not preclude our jurisdiction over the UPSA. Our reasoning is discussed below.

In view of the language in the "but" clause of Section 201(b)(1) that the Commission "shall not" have jurisdiction over facilities used for the generation of electric energy, it is clear that the FPA places a limitation on our authority over generation facilities. However, it is equally clear that Section 201(b)(1) of the Act grants us jurisdiction over the sale of electric energy at wholesale in interstate commerce. We cannot interpret the "but" clause of Section 201(b)(1) as nullifying the authority granted to us in the first sentence of Section 201(b)(1), in situations where generation facilities are used for interstate wholesale sales. To interpret the statute otherwise would be inconsistent with the declaration in Section 201(a) that Federal regulation of the sale of energy at wholesale in interstate commerce is necessary in the public interest. Furthermore, it would permit companies engaging in wholesale sales in interstate commerce to avoid the intended Federal regulation in Section 201(a) by forming a generation-only subsidiary to engage in the wholesale sales which otherwise would come under our jurisdiction. Thus, where the sales made from a generating facility are sales of electric energy at wholesale in interstate commerce, we conclude that under the FPA we retain jurisdiction over those sales.

Our interpretation of the FPA and assertion of jurisdiction over the UPSA are supported by *Hartford Electric Light Co. v. F.P.C.*, 131 F.2d 953 (2d Cir. 1942), *cert. denied*, 319 U.S. 741 (1943). In *Hartford*, the FPC had issued accounting orders directing the company to comply with the Commission's Uniform System of Accounts. Hartford asked the Court of Appeals to set

aside the Commission order, arguing that it was not a "public utility" subject to jurisdiction under the Federal Power Act. Although Hartford sold power and energy to a neighboring public utility, Connecticut Power Company, which in turn sold some of the power and energy in interstate commerce, Connecticut Power Company owned all of the transmission facilities up to the wall bushings on the Hartford generating plant. Hartford argued that facilities were either transmission or generation facilities. Since it had no transmission facilities, it must only have generation facilities, and these were not jurisdictional facilities pursuant to the Federal Power Act. The court, however, took a different view, and affirmed the Commission:

> Section 201(b) confers jurisdiction over not only facilities (1) for interstate *transmission* but also—and—*disjunctively* —over facilities (2) for interstate wholesale *sales*. If the Commission has no jurisdiction under § 201(b) over generation facilities, then that part of that section conferring jurisdiction over facilities for interstate wholesale sales becomes meaningless—unless there is a third category of facilities, i.e., those used neither for transmission nor for generation. We must, therefore, look for that third category. We find it in petitioner's corporate organization, contracts, accounts, memoranda, papers and other records, in so far *(sic)* as they are utilized in connection with such sales. (Citation omitted). 131 F.2d at 961.

The court then found Hartford a "public utility" based on an alternative ground:

> Even if we assume that petitioner has no facilities for interstate transmission, and that petitioner's books, records, etc., are not facilities for wholesale sales in interstate commerce, so that petitioner has nothing except facilities for generation, still petitioner's contention is unsound. For *we consider that generation facilities, where used as aids to such sales, are within the Commission's jurisdiction under § 201(b).* Id. (Emphasis added.)

The Supreme Court in *Connecticut Light and Power Company v. F.P.C.*, 324 U.S. 515 (1945), reversed a lower court's finding that Section 201(b) of the FPA allowed jurisdiction over facilities used for local distribution, and rejected some of the *Hartford* rationale that the lower court had relied upon. However, the Supreme Court also recognized the *Hartford* decision's alternate ground for jurisdiction, specifically noting that the *Hartford* court had recognized the need for finding that the generating facilities in that case were *used as facilities for interstate wholesale sales of electric energy, and were therefore within the jurisdiction of Section 201(b) of the Act.* The lower court in the *Connecticut* case, it noted, had failed expressly to make such a determination. 324 U.S. at 528-29, note 6.

In the instant case, there is no question that the Grand Gulf 1 generation facilities are used as facilities for interstate wholesale sales, since sales made by MSE from those facilities involve sales of electric energy at wholesale in interstate commerce. We thus reject the argument that we have no jurisdiction over the UPSA sales because Grand Gulf is a generating facility not subject to our jurisdiction, or that we have no jurisdiction over MSE because it does not own facilities subject to our jurisdiction.[6]

We next address whether, assuming jurisdiction over the UPSA sales, we have authority to amend the agreement so as to "force" parties to purchase and sell capacity in amounts other than those contractually agreed upon. The APSC/MoPSC and AP&L contend that Judges Head and Liebman made inconsistent rulings in this regard. Judge Head, 30 FERC at p. 65,154, concluded that:

> . . . while it is correct that FERC cannot compel one utility to purchase from or sell to another, *Southern Company Services, Inc.*, 20 FERC ¶ 61,332 (1982), this situation is not

[6]*Cf. Middle South Energy, Inc. v. Arkansas Public Service Comm'n*, Nos. 84-2409, 84-2410, and 84-2480 (8th Cir. Aug. 23, 1985), *aff'g*. *Middle South Energy, Inc. v. Arkansas Public Service Comm'n*, 593 F. Supp. 363 (D. Ark. 1984).

> present in the instant case. The MSU operating companies have not refused to share generating costs but rather the 1982 System Agreement covers how such exchanges should take place and at what rates. The Commission in this proceeding is not dealing with a forced purchase but with the proper method of allocating costs among the affiliated MSU companies, a matter well within FERC's authority. *See Central Iowa Power Cooperative v. F.E.R.C.*, 606 F.2d 1156 (D.C. Cir. 1979), and *Municipalities of Groton v. F.E.R.C.*, 587 F.2d 1296 (D.C. Cir. 1978).

Judge Liebman, 26 FERC at pp. 65,115-16, also relying on *Central Iowa* and *Municipalities of Groton*, and after thoroughly discussing the two cases, rejected the argument that the Commission cannot reassign allocation percentages (and impliedly "compel" purchases). In fact, he found that the *Central Iowa* court had confirmed the Commission's authority to compel additional pool services if a voluntary pooling agreement were found unjust, unreasonable, unduly discriminatory or preferential, and that this finding furnishes direct support for the Commission to reallocate the Grand Gulf percentages in order to correct the discriminatory nature of the UPSA.

In Opinion No. 234, we determined, 31 FERC at p. 61,643, that the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent. On rehearing, LP&L and NOPSI argue that we should adhere to this finding but, as an alternative to the finding, conclude that Section 206(a) authorizes the Commission to establish new terms for a contract found to be unjust, unreasonable, unduly discriminatory or preferential, and that the section imposes no restrictions on new terms dealing with the amount of power purchased and sold.

Although Judge Head concluded that the Commission could not compel a utility to purchase from or sell to another, we do not interpret his decision as applying to cases such as this one, where

we are dealing with contracts involving jurisdictional sales and where it is necessary to "compel" a different purchase in order to achieve just, reasonable, and non-discriminatory rates. To interpret Judge Head's statement otherwise would be inconsistent with his prior conclusion, 30 FERC at p. 65,150, that the Commission's authority under Section 206(a) to order some form of production cost equalization cannot reasonably be challenged, and his statement, 30 FERC at p. 65,151, that the Commission has authority, in exercising its public interest duties under Sections 205 and 206 of the FPA, to assure that the inter-company transactions are just, reasonable, non-discriminatory and non-preferential.

The case cited by Judge Head in making his statement that the Commission cannot compel a purchase or sale, *Southern Company Services, Inc.*, was appropriately distinguished by Judge Liebman and was recognized by Judge Head as involving a factually different situation than the one here. *Southern* involved a unit power sales agreement between Florida Power & Light Company (FP&L) and Southern Company Services (Southern). Seminole objected to the agreement, alleging that if FP&L purchased from Southern rather than Seminole, it could drive Seminole's costs upward and make it more difficult for Seminole to compete with FP&L for retail customers. The Commission rejected Seminole's argument, noting that Seminole had failed to assert that the rates under the agreement were unjust or unreasonable, or that any part of the agreement was unduly discriminatory or preferential.

On rehearing, the Arkansas parties continue to cite *Southern* as standing for the proposition that the Commission has no authority to order a utility to buy from a particular source. As discussed above, the Commission rejected Seminole's arguments on narrower grounds, i.e., that Seminole's broad anticompetitive allegations did not properly assert a violation of the FPA. Additionally, there are two significant distinctions between *Southern* and

the case before us. First, the agreement in Southern was not, as here, among commonly owned affiliates on an integrated system. Second, Seminole was not a party to the agreement being contested, whereas here all of the parties, including AP&L, who have been re-allocated Grand Gulf shares, are signatories to the UPSA.

Based on the above, we do not view the decisions of Judges Head and Liebman to be inconsistent concerning our authority to amend the terms of the UPSA pursuant to Sections 205 and 206. We decline to grant the rather broad request of LP&L and NOPSI that we find that Section 206 "imposes no restriction on new terms dealing with the amount of power purchased or sold." (Rehearing request, p. 3.) However, we wish to clarify that under the circumstances presented by these dockets, we view Sections 205 and 206 as providing authority to change the allocation percentages as necessary to achieve just, reasonable, nondiscriminatory and non-preferential rates, whether or not the central issue is viewed as one of cost allocation or as "forced" purchases.

In reference to the above conclusion, we emphasize that the UPSA cannot be viewed in isolation. It is an agreement which "supplements or supersedes" the coordination arrangements among the MSU utilities,[7] and, as noted by Judge Liebman, is a contract "affecting" rates under the 1982 System Agreement. Given the particular circumstances of this case, we think it clear that we have authority to amend the UPSA and/or the System Agreement pursuant to Sections 205 and 206.

The *Mobile-Sierra* arguments raised on rehearing must again be rejected. The same arguments were adequately addressed and rejected by Judges Liebman and Head, whose discussions we affirmed in Opinion No. 234 and are summarized herein. However, there is one argument on rehearing which we will briefly address. The APSC/MoPSC claim (rehearing request, p. 103)

[7] 31 FERC ¶ 61,304, at p. 61,627 (1985) (Order on remand).

that the rulings of the two judges are contradictory in that Judge Liebman implied that the *Mobile-Sierra* doctrine applies to the UPSA, but Judge Head, 30 FERC at p. 65,147, found the doctrine inapplicable because MSS was not attempting by filing the 1982 System Agreement to change a fixed rate contract.

We disagree with the APSC/MoPSC that the judges' *Mobile-Sierra* findings are contradictory. What Judge Head found at p. 65,147 of his decision was that "the specific ruling in *Sierra* proscribing unilateral contract changes by rate filings, is not applicable." He went on to find that the *Mobile-Sierra* doctrine makes clear that the Commission has the power under Sections 205 and 206 of the FPA to revise a contract that is unjust, unreasonable, unduly discriminatory or preferential, and that the doctrine "does highlight the authority of the Commission to approve the 1982 System Agreement as filed, or to revise it if to do so is in the public interest." *Id.* Judge Liebman likewise recognized that the *Sierra* case focused on a situation where a public utility unilaterally was attempting to increase a fixed rate contract with a customer. 26 FERC at p. 65,114. He further found, however, as did Judge Head, that the *Mobile-Sierra* doctrine does not say that a voluntary contract can never be modified to rectify a statutory violation such as undue discrimination. *Id.* We fail to see how these interpretations or rulings are contradictory.

We have concluded in these dockets that the 1982 System Agreement and the UPSA, as filed, would result in rates that are not just, reasonable, and non-discriminatory, and we have determined new rates and amended contracts to remedy this. We, therefore, have complied with the statutory authority granted to us under Sections 205 and 206 of the FPA.

One last matter to be addressed concerning jurisdiction is a request by AI that the Commission clarify its discussion at p. 61,643 of Opinion No. 234 concerning Federal preemption and *Arkansas Electric Cooperative Corp. v. Arkansas Public Service*

Comm'n, 461 U.S. 375 (1983). AI states that our Opinion apparently equates the concepts of "jurisdiction" and "preemption" and contends that, "Surely, despite its broad assertion of federal preemption, the Commission is not suggesting that Congress meant for it to dominate the field of electric power regulation to the total exclusion of the states." (Rehearing request, p. 2.) AI asks the Commission to clarify its position or delete its reference to preemption.

AI totally misconstrues our opinion if it reads the Opinion as implying that the states have no jurisdiction in the field of electric power regulation. Several parties had cited the *Arkansas* case as supporting broader state jurisdiction over electric rates. The intent of the cited language in our opinion was to distinguish the case from the instant situation and to clarify that the case did not restrict this Commission's clear jurisdiction over sales of electric energy at wholesale in interstate commerce under Section 201(b) of the FPA. Judge Head appropriately considered the *Arkansas* case, 30 FERC at pp. 65,150-51, and we concurred in his discussion of the need to balance Federal and state interests in exercising our jurisdiction. Furthermore, we think our opinion, taken as a whole, as well as Judge Head's discussion, which we adopted, clearly recognize the role of the states in regulating retail electric rates and the need to balance overlapping state and Federal electric rate jurisdiction.

The other jurisdiction arguments made on rehearing are, in general, repetitive of ones already made and considered on exceptions and were adequately addressed in those portions of the initial decisions which we affirmed in Opinion No. 234, or in the opinion itself.

State/Federal Relationship

Related to the above arguments concerning the line between state and Federal jurisdiction over rates is the general argument that the Opinion destroys effective state regulation of retail rates. Major arguments in this regard are discussed below.

The APSC/MoPSC argue on rehearing that equalization of nuclear generation costs amounts to setting equalized retail rates among MSU affiliates, and that it flies in the face of Judge Head's conclusion (adopted in the Opinion) that the Commission has no jurisdiction over generating facilities. They claim that the Opinion has effectively emasculated the decisions of the APSC as to need for generating facilities, value of those facilities, return on AP&L's investments, and AP&L's level of operating costs. They further argue that the effect of the decision is to: remove from rate base at the state level all of the nuclear plants of the operating companies; eliminate from APSC jurisdiction and transfer to FERC jurisdiction most of AP&L's base load power; and remove from APSC regulatory power essentially all control over capacity costs on the AP&L system. The decision, they claim, reflects no balancing or weighing of state interests. The APSC/MoPSC also argue that the ordering of equalization of all nuclear generating costs ignores and is inconsistent with Judge Head's reasoning, adopted by the Commission, for refusing to order systemwide production cost equalization.

The Cities of Conway, *et al.*, argue that production cost equalization would impinge on state regulatory jurisdiction, and strain the State/Federal relationship. They claim that to allow the Commission, through production cost equalization, to force additional rate base and generating facilities on AP&L without prior APSC approval would be contrary to Section 201 of the FPA.

AMAX, Inc., argues that the Opinion will work major changes in AP&L's retail rate base, and result in FERC regulation of generating facilities by transferring local costs from state to state. Further, claims AMAX, the states would be precluded from judging the prudence of Grand Gulf costs and denied any say in the rate of return imposed as part of these costs. AMAX contends that cost equalization would have a significant effect on state commissions planning for future power plant construction.

The MPSC and the Attorney General of the State of Mississippi argue that the Commission's decision is contrary to *Pacific Gas and Electric Co. v. State Energy Resources Conservation and Development Comm'n,* 461 U.S. 190 (1983),[8] in that it impinges on the states' paramount authority in certification decisions regarding need, type, and costs of construction of new generating facilities.

The above arguments must be rejected. Contrary to the assertions or implications made on rehearing, the Commission's Opinion is the result of a careful balancing of the state and Federal interests involved. Our Opinion, 31 FERC at p. 61,344, explicitly adopted Judge Head's discussion, 30 FERC at pp. 65,148-51, in which he found that the Commission has jurisdictional authority to order a form of production cost equalization, but concluded that exercise of this jurisdiction must be tempered and weighed against the policy consideration that generation facilities and retail rate regulation should be left to the states, and that cost equalization should be ordered only if necessary to ensure just, reasonable, and non-discriminatory agreements governing transactions among the MSU subsidiaries. While we disagreed with Judge Head's decision to a certain extent, the interests of the states involved in this case weighed heavily in favor of our decision *not* to adopt full production cost equalization. We thus find our decision fully consistent with the reasoning of Judge Head concerning the need to pay careful heed to the impact our decision would have on the states.

An important point to be emphasized here is that our decision was a limited one. Contrary to the implication of the Cities of Conway, *et al.*, we did not order production cost equalization. Nor did we order equalization of all nuclear generation costs, as indicated by the APSC/MoPSC. Opinion No. 234 requires

[8]Numerous parties opposing any form of cost equalization cited this case in the proceedings below and on rehearing. The case was specifically addressed at p. 61,644 of our Opinion.

equalization only of nuclear *investment* costs. The result of the Opinion, contrary to the assertion of the APSC/MoPSC, is not equal *rates* for all MSU affiliates. While our decision may increase the System costs subject to FERC jurisdiction, the record is unclear as to the extent this would occur since a substantial portion of System costs are already subject to our regulation.[9] The basic nature of regulatory control retained by the states under previous System agreements remains unchanged. What our decision attempts to do is amend the filed agreements to achieve a non-discriminatory sharing of excess capacity cost imbalances on the integrated System, consistent with the goal of the System Agreement, and to do so with as little intrusion on the States as possible.

Integrated Nature of MSU System

Several parties mischaracterize or misconstrue the Commission's findings concerning the integrated nature of the MSU System. They characterize the Opinion as one which finds the MSU System to be a single, "monolithic" entity, which does not consider all relevant evidence as to autonomy on the part of the individual operating companies, and which ignores evidence con-

[9]For example, Judge Head indicates, 30 FERC at p. 65,149, that *full* production cost equalization (which was *not* adopted here) would remove from the state commissions control of the vast majority of the cost of rendering service within each jurisdiction, and that Staff's full production cost equalization proposal would subject more than 75% of rate base to FERC jurisdiction (citing ER82-483 APSC Ex. 2, pp. 46, 47). (APSC Ex. 2 is the direct testimony of APSC witness Alvin J. Roe.) Other parties, for example OCC and Georgia Gulf, rehearing request, p. 6, claim that more than half of the total costs allegedly "transferred" to FERC jurisdiction under production cost equalization are or would be subject to FERC jurisdiction even absent production cost equalization (citing ER82-483 MPSC Ex. 24). (MPSC Ex. 24 is a 1979 letter to the chairman and chief executive officer of MSU from the president and chief executive officer of LP&L, concerning the advantages and disadvantages of proposed plans to modify the System Agreement.)

cerning individual company planning, financing, operation, and actual ownership of System generation units, and representations to state commissions concerning those units.[10]

Both AI and the Cities of Benton, *et al.*, question whether the Commission intends the term "single system" to mean "a group of utilities that have submerged their separate identities, and the interests of their native-load ratepayers, into a common, homogenous physical and economic unit that is indistinguishable from a single utility."[11]

We think it obvious from Opinion No. 234 that the Commission did not intend a meaning such as that quoted above. The Opinion does not describe the MSU System as a "monolithic" entity, nor does it ignore certain autonomous aspects of the individual operating companies.[12] Contrary to the claims of the APSC/MoPSC, AP&L, and the Cities of Conway, *et al.*, the Opinion does not find that all activities of the System and the individual operating companies are controlled by the MSU Board of Directors, nor does it misunderstand the relationship of the companies and the various boards of directors within the System. The Opinion, 31 FERC at pp. 61,645-51, incorporates Judge Head's accurate and thorough description of the interrelationship and overlapping officers and directors among MSU and its sub-

[10]Some or all of these characterizations are made by AI, the APSC/MoPSC, the Cities of Conway, *et al.*, the Cities of Benton, *et al.*, AP&L, and the MPSC.

[11]AI rehearing request, p. 18. The rehearing request of the Cities of Benton, *et al.*, at pp. 7-8, contains an almost identical definition.

[12]The Opinion itself does not even use the term "single system." To the extent Judge Liebman refers to Middle South as a "single" system (*e.g.*, at p. 65,110 of his decision), we do not agree that this implies that there is absolutely no autonomy on the part of the individual companies or that the MSU Board of Directors has total control over the companies.

sidiaries,[13] and concludes that the MSU Operating Committee (*not* the MSU Board of Directors) makes *major* critical decisions on the System, *primarily* for the System as a whole.

In reaching the above conclusion, the Opinion repeatedly recognizes that the individual operating companies are intimately involved in the planning stages of new generation units on the System. It further recognizes that the Operating Committee (which is composed of representatives of the individual operating companies) makes major System decisions in the form of recommendations to the chief executive officers who, in turn, vote on the recommendations, and that the individual companies make final specific decisions necessary to carry out the overall System plan.[14] This interaction is summed up in the major findings listed at p. 61,650 of the Opinion.

The APSC/MoPSC contend that the Commission relied on selective testimony in finding that the MSU System is a "monolithic" entity, and that the operating companies do not function according to a pattern of autonomy. They claim that the Commission erroneously concluded that a lack of complete autonomy was equivalent to absence of *any* autonomy. AP&L also claims that the Commission's findings are inconsistent with the record and, in this regard, argues that the Commission improperly interpreted Mr. Lupberger's statement (ER82-616 Tr. 347) that the System is operated as though it were one electrical system under one ownership. This statement referred only to the fact that the units are operated by central dispatch, claims AP&L, and a requirement to pool nuclear investment cannot be predicated on the mere fact that companies use central dispatch.

We disagree strongly with any implication that the testimony relied on in the Opinion is not representative of what is contained in both records concerning the operation of and decisionmaking

[13]We note that p. 61,646 of the Opinion refers to Judge Head's description as being located at 30 FERC pp. 63,141-43. This is a typographical error which should be changed to 30 FERC pp. 65,141-43.

[14]For example, specific timing and location of new generation.

on the MSU System. A reading of the testimony cited in the Opinion does not reflect a "monolithic" entity, but recognizes the role of the individual companies in System decisionmaking, and the interplay between System and individual company needs. Furthermore, the Commission did not conclude that a lack of complete autonomy was equivalent to the absence of *any* autonomy. We think it clear from our discussion in the Opinion and the evidence cited therein that we were not concluding that the operating companies have no role in decisionmaking and absolutely no autonomy. To the extent any party infers otherwise, the preceding discussion should serve to clarify our position. The fact that there may be *some* autonomy on the part of the individual companies, however, does not lead us to conclude that there is a "pattern of autonomy" such that the individual companies have complete independence and are not subject to major decisions on the System, particularly as to generation additions, being made by and for the System as a whole.

As to AP&L's argument concerning specific testimony of Mr. Lupberger, the reference to that testimony was not intended to imply that Mr. Lupberger was referring to anything other than the physical operation of the System. We further think it is obvious from reading the Opinion as a whole that our decision was not, as argued by AP&L, predicated on the mere fact that the companies use central dispatch.

AP&L also argues that, contrary to Opinion No. 234, there is at least one instance where a company (LP&L) refused to build a unit despite a recommendation to do so by the Operating Committee. The evidence cited by AP&L, however, consists only of Operating Committee minutes showing that the Committee recommended that LP&L build coal units in Northern Louisiana in the early 1980's, and testimony by J.D. Phillips, a senior vice president of AP&L, that there was never any activity regarding

these units.[15] This does not reveal an actual refusal to build the units. AP&L cites no evidence as to the reason the units were never constructed.

The APSC/MoPSC contend that the Commission ignored evidence and judicial precedent, relied on by Judge Head, concerning the "pattern of autonomy." Specifically, they claim that we ignored Judge Head's review of decisions by the SEC, AEC, Atomic Safety Licensing Board, the FPC and the FERC, and his conclusion, 30 FERC at p. 65,161, that prior characterizations of the integrated MSU operations do not dictate production cost equalization. They claim that the Opinion also ignored Judge Head's discussion, 30 FERC at pp. 65,162-63, concerning the fact that in Arkansas State proceedings AP&L was required to justify the need for new facilities to meet Arkansas requirements.

Judge Head concluded, 30 FERC at p. 65,161, that "the mosaic of Federal agency decisions relating to the Middle South system leaves no doubt that the system is a closely integrated and coordinated power pooling arrangement from a planning, construction and dispatch standpoint." He concluded that although this finding conceptually lends support to an equalization rationale, it does not of itself constitute such an overriding consideration that it *requires* production cost equalization. We do not consider our decision inconsistent with Judge Head's findings and conclusions in this regard. Our Opinion did not order production cost equalization, and it fully considered the same factors weighed by Judge Head in determining how best to achieve just, reasonable, and non-discriminatory rates. In reference to the representations made in Arkansas State proceedings concerning AP&L's need for new facilities, our Opinion explicitly recognized these at p. 61,652.

A minor point raised by the APSC/MoPSC concerning our refusal to find that the operating companies are autonomous is our reference at p. 61,651 of the Opinion to the fact that the 1982

[15]ER82-483 Tr. 1200-02; OCC Exh. 23. p. 7; OCC Exh. 24, p. 4; OCC Exh. 26, p. 16; OCC Exh. 30, p. 2.

System Agreement was changed to provide for decisions by majority vote rather than a two-thirds vote, in order to ensure that one company cannot block a Committee decision.[16] The APSC/MoPSC argue that the Commission fails to note that two companies can still exercise their autonomy to block Operating Committee decisions and that MSS has only a 20% vote such that it cannot impose its will on the Committee. We fail to see the relevance of this argument, since the point to be made is than an *individual* company does not have sufficient autonomy such that it can block a decision against the wishes of other Operating Committee members.

AI, the APSC/MoPSC, and AP&L argue that our decision was made without regard to actual ownership, construction, financing, and operation of generation units, and that it ignores the fact that plant additions other than Grand Gulf become the exclusive asset and economic responsibility of the owning company. They further claim that we ignored the history of AP&L's capacity construction and the fact that it received no financial assistance from other companies when it had financing difficulties with its White Bluff and Independence coal units. Related arguments made by AI and Cities of Benton, *et al.*, are that two provisions of the System Agreements *guarantee* the economic individuality of the MSU subsidiaries under the System's pooling practices: (1) the requirement that each company must normally provide its own generating capacity, or contract for capacity, adequate to meet its native load; and (2) the rule that under economic dispatch, while each company agrees to have all system units dispatched in order of efficiency, each pool member has first call on the power and energy produced by its own units.

The Arkansas parties are incorrect that our decision was made without regard to ownership and financing of generating units.

[16]To clarify any confusion concerning the testimony cited in our discussion as Tr. 84-85, this refers to LPSC Ex. 86 pp. 84-85, which consists of transcript pages from an MSS proceeding in Docket Nos. ER81-428-000 and EL81-12-000.

The Opinion explicitly recognized, 31 FERC at pp. 61,649 and 650, that each operating company is required by the System Agreement to own or purchase capacity to meet native load. We also recognize, although it was not emphasized in the Opinion, that pool members have first call on the power and energy produced by units which they own. All of these factors were important considerations in our decision not to adopt full production cost equalization, and, to the greatest extent possible, to allow the individual companies to retain the benefits of units which they have been responsible for constructing.

In reference to the parties' claim that pool members are independent because they finance their own construction, two other points should be made. It cannot be ignored that each operating company is financially a part of and dependent on MSU, which supplies equity funds as needed to complete a construction project. A recent example of the financial interdependence of the MSU Companies is Standard and Poor Corporation's lowering of debt issues of *four* MSU operating companies amid signs that *two* of the units face liquidity problems and that systemwide financial stress is likely to continue.[17] Moreover, page 123H of AP&L's 1982 Form No. 1 indicates that the company now participates with certain other companies of the Middle South System in a System money pool arrangement whereby those companies with available funds make short-term loans to other companies in the System having short-term borrowing requirements.

Another argument concerning the operating companies' responsibility for financing their own construction was raised by MP&L. MP&L contends that the Commission erroneously dismissed MSE's role in the System's operation, and erred in finding (Opinion at p. 61,654) that there was no reason to believe the System would not have taken steps similar to those it took for Grand

[17] *The Wall Street Journal*, April 26, 1985; *Standard and Poor's Creditweek*, April 29, 1985, p. 10, and May 6, 1985, pp. 21-25.

Gulf had other units experienced the same financial problems. MP&L claims this is inconsistent with uncontroverted record evidence to the contrary. In support, MP&L states that in 1975 and 1980, AP&L experienced severe financial difficulties in completing the coal-fired White Bluff and Independence units, and the System did not transfer the projects to MSE or otherwise provide financial assistance to AP&L. As a result, claims MP&L, AP&L was forced to stop construction until it could obtain the necessary financing itself.

We fully recognize that the operating companies historically have financed units located in their respective states without direct financial assistance from other System companies. However, there has been no showing that any company previously experienced the magnitude or type of problems associated with Grand Gulf, or was totally unable to finance a unit, as was the case with Grand Gulf.[18] Moreover, the formation of MSE was consistent with the purposes of the integrated MSU power pool operations as embodied in the System Agreement.

The Arkansas parties[19] argue that the Commission's Opinion erroneously "pierces the corporate veil" by disregarding the separate corporate identities of the four operating companies, and used the wrong standards for doing so. They claim that such an extraordinary measure requires a showing that corporate separateness is nothing more than a sham, that the corporate existence has been abused or manipulated to evade the law or gain some advantage contrary to public policy, or that MSU has used the separate corporate identities of MSE to frustrate or avoid any

[18] It is true that the Grand Gulf financing problems differentiate that unit from others on the System. We nevertheless do not think it appropriate, as argued by some parties, to equalize only the cost of Grand Gulf, since Grand Gulf originally was planned in the same basic manner as other nuclear units on the System, and all System nuclear units were planned to help meet the overall System goal of achieving a new fuel mix.

[19] The Cities of Benton, *et al.*, AI, AP&L, the Arkansas and Missouri Congressional Delegations, and the Cities of Conway, *et al.*

purpose of the FPA. Many of the parties cite *Nantahala Power and Light Co.*, Opinion No. 139, 19 FERC ¶ 61,152 (1982), as defining the criteria for piercing the corporate veil. They also argue that the Commission based its decision solely on the fact that the operating companies are commonly owned.

We do not view our decision as one involving a formal "piercing of the corporate veil" and consider *Nantahala* to be distinguishable in this regard. *Nantahala* involved a non-jurisdictional entity, Aluminum Company of America (Alcoa), and two subsidiary utilities, Nantahala and Tapoco, Inc. Nantahala served as a public utility while Tapoco was an industrial power supply source for Alcoa. In a complaint proceeding before us, a Nantahala customer had claimed that Alcoa had used its subsidiaries for its own benefit, by diverting for its private use hydroelectric power dedicated to public service. The customer claimed that all three companies had violated the FPA, and asked the Commission to pierce the corporate veil between the two subsidiaries and treat them as one entity for ratemaking purposes. We refused to do so because there was no evidence that Alcoa had used the separate corporate identities of the two subsidiaries to frustrate the purposes of the FPA, *or* that the companies operated as an integrated system.

The facts of *Nantahala* are clearly distinguishable from those here. The question before us is not whether MSU has used the separate corporate identities of the operating companies to frustrate the purposes of the FPA. Rather, the issue is how to achieve just, reasonable, non-discriminatory and non-preferential rates among highly integrated companies, pursuant to jurisdictional pooling agreements which have been filed with us. Our decision does not, as argued by some parties, rest on the mere fact that the operating companies are commonly owned. However, because of the nature of the MSU System, and the types of agreements before us, any resolution cannot ignore the interrelationship of the MSU companies, particularly regarding System decision-making, or the interrelationship of the agreements governing pooling transactions.

AI, the Cities of Conway, *et al.*, and the Cities of Benton, *et al.*, argue that in finding MSU to be a "single system," the Commission misjudged the nature of the System and its coordinating agreements. They claim there is no evidence to suggest that the actions of the operating companies differ materially from those of unaffiliated utilities that elect to interconnect, economically dispatch generating facilities, and engage in joint reserve planning. The fact that the operating companies are commonly owned, they argue, does not convert actively coordinating systems into a single system. We think these arguments are misplaced. The case before us involves affiliates, and we would be remiss to ignore this fact in reviewing transactions and agreements among those affiliates. The types of transactions that take place among interconnected non-affiliates is not before us and is not relevant to our consideration here. Moreover, our decision does not hinge on the single factor of common ownership, but rather focuses on a variety of factors including the manner in which decisions are made by the commonly owned affiliates, and for whose primary benefit those decisions are made.

Lastly, we address the arguments of AP&L, the Cities of Benton, *et al.*, the APSC and AI, that if the operating companies operate as a single entity, then the presence of wholesale transactions vanishes, any transfer of power among the companies becomes an intracompany transfer, and Commission jurisdiction is voided. As previously discussed, our Opinion does not find MSU to be a single, monolithic entity, with total disregard for the existence of the individual operating companies. The transactions under both the System Agreement and the UPSA clearly are sales for resale in interstate commerce, despite the fact that the companies operate a physically integrated system and plan construction primarily to meet the needs of the System as a whole, and they remain subject to our jurisdiction.

The Opinion No. 234 Allocation

On rehearing, almost all parties object to the Grand Gulf allocation adopted in Opinion No. 234. To the extent the arguments of the parties may not have been adequately addressed in the Opinion or in portions of the initial decisions adopted in the Opinion, the major arguments are addressed below.

AP&L argues that the filed UPSA is a rational disposition of Grand Gulf power, based on recognized power planning principles. The result of nuclear investment cost equalization, claims AP&L, would be that the production costs of each company would no longer be based on actual investment and expenses incurred by the company to serve its customers, but instead on the company's own fossil fuel unit costs and an average of the investment for all nuclear units. The resulting rates for AP&L would not bear a direct relationship to its actual investment and expenses. AP&L further argues that the Opinion is inconsistent with the purpose and effect of prior coordination agreements and Commission precedent, that equalization has never been an objective of the System Agreements, and that the FPA does not require equalized costs.

The APSC/MoPSC also support the filed UPSA, and contend that the Commission undertook no in-depth analysis of the unit sales plan with respect to the appropriateness of the plan from a power supply standpoint. They argue that the allocation was improperly made from the perspective of 1983 rather than from the more appropriate 1979-80 time frame when the unit sales plan was adopted. The analysis, they contend, should be based on a 1979 perspective and focus on: the objectives in making the sales of Grand Gulf entitlements; whether those objectives were just and reasonable; and whether the sales agreement serves those objectives. The APSC/MoPSC further contend that the Commission erroneously concluded that one of the System goals was to equalize generating costs, and that the allocation adopted is in error because it ignores coal, gas and hydroelectric capacity on the System and does not serve System goals.

Contrary to the APSC/MoPSC's contention, and the implication of AP&L, our Opinion did not conclude that a goal of the MSU System was to equalize generating costs. Rather, it specifically noted, at p. 61,646, the intention of the System Agreement to provide a basis for equalizing among the companies any *imbalance* of costs associated with the construction, ownership, and operation of such facilities as are used for the mutual benefit of all the companies. The Opinion also recognized, at pp. 61,646 and 61,656, all of the major goals and objectives of the System Agreement, including the power supply goals of moving toward a new fuel base of coal and nuclear power and having each company obtain a proportionate share of base load generating units either by ownership or purchase. Our decision, at p. 61,656, specifically found the adopted allocation would be consistent with and promote the System's major objectives.

We disagree with the APSC/MoPSC's contention that the allocation should have been made from the perspective of the 1979-80 time frame when the UPSA initially was adopted. The salient issue here is not whether the agreement was reasonable when made, or whether it met the System objectives at the time it was made. Rather, the principal inquiry is whether the allocation is appropriate based on the evidentiary record that was subsequently developed. In this particular case, we are dealing with a situation involving changing factors unique to nuclear plant construction, and the hearing in ER82-616 was to set rates for a unit which had not yet gone into commercial operation. We therefore think it was entirely appropriate to focus on the more recent record data in the ER82-616 proceeding for the specific purpose of apportioning Grand Gulf costs under the UPSA.

In reference to AP&L's argument that the adopted allocation will result in costs no longer based on actual investment and expenses, it is true that individual companies will be responsible for portions of a unit in which they themselves did not actually invest. The point is, however, that if a unit is built to meet overall System

goals, then the individual company will benefit from that unit either directly or indirectly, and may properly bear a portion of the costs of the unit. Further support for an allocation that is not based strictly on a company's own investment and expenses in these proceedings is the individual company's contractual agreement (the System Agreement) to bear a portion of any imbalance of costs resulting from such a unit.

Several Arkansas parties argue that the Commission erroneously imposed a Grand Gulf allocation on AP&L without finding that AP&L *needed* such capacity.[20] In this regard, AI and the Cities of Benton, *et al.*, also contend that the Commission erred in relying on AP&L's former involvement in the Grand Gulf project, but disregarding AP&L's limited contractual obligation to purchase Grand Gulf power on an as-needed basis. AP&L's obligation, they state, was only to take such amount of Grand Gulf as it needed, as determined by whether it was "long" or "short" under the MSU System Agreement. They claim the Commission disregarded the set of amended agreements and enforced the original ones, oblivious to the fact that AP&L had, at a maximum, bargained for no more than a small percentage share of Grand Gulf.

The argument that allocation of Grand Gulf costs should be based on whether individual companies "need" Grand Gulf capacity must be rejected. We reaffirm that the Middle South companies appropriately approach power planning on a system-wide basis, whereby the individual companies' needs are the component parts of the System power plan. Implementation of the System plan, however, requires that the individual companies' needs be subsumed by the greater interests of the entire System. Moreover, the System Agreement requires an equitable sharing of cost imbalances associated with facilities used for the mutual

[20]AI, the Arkansas and Missouri Congressional Delegations, the Cities of Benton, *et al.*, and the APSC. The MLSC also raises this point as it relates to Mississippi ratepayers.

benefit of all companies. The record evidence relied upon in Opinion No. 234 establishes that Grand Gulf was built primarily to serve the System as a whole and to meet the System goal of obtaining a greater proportion of nuclear capacity. Our task, therefore, is one of allocating costs consistent with the mandate of the Federal Power Act, and the allocation of Grand Gulf power must rest not on the "needs" of an individual company, but rather on the principles of just, reasonable, non-discriminatory, and non-preferential rates. Opinion No. 234 follows the mandate of the FPA and is consistent with the intent of the System Agreement.

The Mississippi parties[21] contend that Opinion No. 234 fails to examine the impact and inequities of the adopted allocation on Mississippi ratepayers, and provides no rate relief for those ratepayers.[22] They also claim that if the Commission accepts Judge Liebman's findings that the filed 31.63% Grand Gulf allocation to MP&L would cause MP&L's rates to increase "dramatically" and cause "serious detriment" to Mississippi ratepayers, then the 33% allocation to MP&L adopted in the Opinion (and by Judge Liebman) is even more detrimental. If 31.63% is unjust and unreasonable, they contend, then 33% cannot be just and reasonable. They further argue that the Opinion will impose unlawful cross-subsidization among the companies. In this regard, the Mississippi Attorney General specifically argues that MP&L would be subsidizing companies with deficient capability responsibility

[21]MI, the MPSC, Representative Webb Franklin, the Attorney General of Mississippi, MP&L, and the MLSC.

[22]MP&L claims the decision will result in costs to MP&L that will be approximately 125% of the average system costs, that MP&L will pay $2,156 per kW for service from the same MSU nuclear units that will serve AP&L for $848/kW, and that the adopted allocation discriminates against three of the operating companies in favor of AP&L. Representative Webb Franklin claims the decision will result in MP&L paying more than 2.5 times as much per kW for nuclear capacity as would AP&L. The MLSC claims the decision will result in pricing electricity beyond the means of the average elderly or poor person in Mississippi, and will render the concept of "universal service" in Mississippi null and void.

since, as a long company, MP&L would be required to take and pay for the high capital costs of Grand Gulf and sell its excess generation at a price based on the low capital costs of its oil and gas-fired generation.

Related to the above arguments is the contention of some of the Mississippi parties that the adopted allocation is discriminatory because it does not result in each operating company bearing the same cost per kWh for Grand Gulf energy, and results in different prices to similarly situated customers despite the fact that the seller's costs are the same.[23] MP&L and Representative Webb Franklin argue that Judge Head's allocation is more equitable because it would result in each customer bearing identical costs per kWh for Grand Gulf energy. MI also claims discrimination on the ground that the adopted allocation ignores the disparity in the size of the MSU operating companies.[24]

Another related argument made by MP&L, the MAG, and MI is that the Opinion erroneously results in allocating costs of the nuclear units, but not associated benefits.[25] MP&L also claims that the decision ignores the disparities in the costs of non-nuclear capacity, and that limiting relief to nuclear units unfairly excludes MP&L from the low busbar costs of energy from the lower-cost conventional plants of the system. A proper rolled-in

[23]MP&L, Representative Webb Franklin, MI, and the MPSC.

[24]In support, AI states that an allocation of $1 of Grand Gulf costs to LP&L would be spread over three times as much customer demand as an allocation of $1 of such costs to MP&L, yet the Commission would allocate over twice as many dollars to MP&L as to LP&L.

[25]The MAG claims that the cost of System nuclear capacity to the companies will range from a low of $804/kW for AP&L to a high of $2,222/kW for NOPSI and MP&L, while the average cost of such capacity was $1,344/kW. (These figures are based on the MAG's Schedule 1 attached to his request for rehearing.) He claims that MP&L would be paying to receive entitlement to 612 MW of nuclear capacity but would actually receive only 370 MW, whereas AP&L would pay for 1,344 MW but would receive 2,245 MW of nuclear entitlements.

cost allocation, claims MP&L, would assign each company a proportionate blend of high and lower nuclear costs in the same proportion as that customer obtains the benefits of the facilities.[26]

The City of New Orleans similarly contends that the decision fails to definitively indicate its impact on the individual companies and their consumers, that it erroneously allocates the costs of nuclear investment while failing to provide matching benefits,[27] that it is discriminatory because it does not result in each consumer paying the same rate for allocated capacity as is paid by every other consumer, and that it discriminates against the smaller MSU companies.[28]

First, we wish to clarify that our intent in adopting a form of very limited cost equalization was not to eliminate all cost disparities on the MSU System or to have the companies necessarily pay the same average cost per kWh for all of their energy. It is true that costs were roughly equalized among the companies under previous operating agreements, although there has never been a stated intent to equalize all costs. As previously recognized herein, the intent of the System Agreements has not been to specifically equalize costs, but rather to equalize any imbalance of costs associated with facilities used for the mutual benefit of all the

[26]MP&L claims that it will pay some 15% of the aggregate cost of all four nuclear units, but receive the benefit of 9.5% of System nuclear capacity.

[27]In support, CNO states that the Opinion's approach will result in a 2.7¢/kWh difference between the highest (NOPSI) and lowest (AP&L) cost companies, as compared to 2.4¢/kWh under Judge Head's decision. It also claims that under Opinion No. 234, NOPSI will bear an 8% share of nuclear investment costs but receive only 4.8% of the capacity produced and energy generated by that total nuclear investment; MP&L will bear 15% of the cost but receive only 9.5% of the benefits; and AP&L will bear 33% of the costs but receive 53.5% of the benefits.

[28]CNO argues that the smaller companies, NOPSI and MP&L, will be discriminated against because they will receive energy only from Grand Gulf, while AP&L will continue to receive all of the ANO 1 and 2 energy, and LP&L will receive all of the Waterford 3 energy.

companies. Where different state regulatory bodies give different treatment to various rate elements, it is a natural consequence that retail rates among the companies will differ. This would be true even under full production cost equalization. What our decision purports to do is to eliminate drastic rate disparities at the wholesale rate level which are associated with units used for the mutual benefit of all companies, and to do so in a manner which disturbs the historical operation of the System as little as possible, and which allows the individual companies to retain as fully as possible the benefits of units they have financed and constructed. In other words, we have sought to achieve an equitable balance between the interests of the individual companies and the System as a whole, consistent with the System Agreement.

We reject the arguments that our allotments of Grand Gulf cause price or other discrimination because they produce a different Grand Gulf cost or price per kWh for each operating company, whereas Judge Head's approach produces a non-discriminatory, uniform Grand Gulf cost per kWh. These allegations of discrimination are unfounded because they are based on references to the *total* kWh's (i.e., kWh's not only from Grand Gulf but from all sources) for each operating company rather than Grand Gulf kWh's. Of course, the rate for Grand Gulf service applies only to Grand Gulf kW's and kWh's.

Our responsibility is to set just, reasonable, and nondiscriminatory rates at the wholesale level. The fact that the Grand Gulf allocation adopted by us may result in ultimate costs per total kWh which are different for each operating company does not constitute undue discrimination at the sale for resale level. Opinion No. 234 adopted a Grand Gulf allotment method designed to equalize the total cost of all nuclear investment per kW of total average demand for each operating company. The resulting Grand Gulf kWh sales will be uniformly priced to each operating company in terms of Grand Gulf kWh's of energy. There is no price discrimination because there is a single formula rate in effect for all

transactions, and each Grand Gulf kWh will cost each operating company the same amount. No other proposal equalizes the total nuclear investment cost per kW of average demand and uniformly prices Grand Gulf kWh's.

The adopted allocation will have a substantial impact on all four of the operating companies, not just on Mississippi. We recognize that there may be an inconsistency in Judge Liebman's finding, 26 FERC at p. 65,107, that the filed 31.63% UPSA allocation to MP&L would cause serious detriment to the Mississippi (and Louisiana) ratepayers, and his ultimate conclusion that MP&L should be allocated 33% of the UPSA. Judge Liebman's decision did not directly address this alleged discrepancy. However, a careful reading of his discussion concerning the discrepancy in rates indicates that the largest discrepancy under the filed UPSA would be as to LP&L,[a] and that his focus appeared to be primarily on LP&L. Whether or not there is a discrepancy in the judge's findings, we wish to clarify that we consider a 33% allocation to MP&L to be equitable, particularly in view of the fact that the result of the Opinion is that all three major geographical areas served by the MSU System will share similar Grand Gulf cost burdens: AP&L—36%; MP&L—33%; and LP&L/NOPSI—31%.

We disagree that the allocation will result in unlawful cross-subsidization. The Grand Gulf allotments represent each company's *pro rata* share of the responsibility for meeting the System goal of moving away from oil and gas toward a new fuel base of nuclear and coal generation. In this regard, we also reject the arguments made by Mississippi parties and CNO that we have

[a]Preceding Judge Liebman's statements is a table which shows that MSE's proposed allocation of Grand Gulf 1 (the filed UPSA) would result in the parties having responsibility for total nuclear capacity (including Waterford 3) in the following amounts: AP&L—$0.9 billion; LP&L—$3.4 billion; MP&L—$0.8 billion, and NOPSI—$0.7 billion.

erroneously focused only on nuclear generation.[a] While we recognize that the System goal was to move toward coal as well as nuclear base load generation and that energy from the ANO nuclear units may be less costly than that from some coal-fired units, we nevertheless think it appropriate to focus only on nuclear units because of the unique nature of and industry-wide problems associated with nuclear construction.

MP&L argues that the cost escalations of Grand Gulf 1 and Waterford 3 might justify focusing exclusively on them, but that they do not support distinguishing the lower cost ANO 1 and 2 units from the coal-fired base load units. CNO similarly argues that the ANO units are not of the same cost caliber as Grand Gulf, but further argues that the fact that some plants are enormously expensive does not justify equalization. Although it may be true that the ANO nuclear units are not of the same cost magnitude as the newer nuclear units, we think it appropriate not to attempt to segregate the nuclear units, particularly in view of the fact that to a great extent it was simply a matter of timing as to which company built the first cheaper nuclear units.

In reference to the arguments that the Opinion erroneously results in allocating nuclear costs but not associated benefits, a major objective of our decision was to fairly apportion nuclear investment responsibility and to do so via appropriate Grand Gulf allotments. We do not think it proper, unless necessary to achieve

[a]MP&L and MI argue that the cost of energy from the ANO units is less than that from recently built coal-fired units on the System, and that the exclusive focus on nuclear generation is erroneous. MI asserts that the adopted allocation will not promote the System's objective to move toward coal *and* nuclear generation.

MI, MF&L and Representative Webb Franklin claim that if all plants are "system" plants, then it is inconsistent not to equalize all production costs. MP&L also argues that the exclusion of coal, gas, and oil-fired units implies that those units separately serve a different customer group than is served by the MSU nuclear units.

just, reasonable, and non-discriminatory results, to re-apportion the benefits of the older nuclear units which have been in service for some time and have already been absorbed by AP&L's native load. As to the Grand Gulf allotments themselves, the companies will receive the benefits associated with the costs they pay for Grand Gulf.

Several Louisiana parties generally support the Commission's findings and conclusions, but argue that we erred in failing to adopt full production cost equalization.[b] OCC and Georgia Gulf argue that the Opinion incorrectly found that production cost equalization would be a substantial change from previous System cost allocation. We disagree. Full production cost equalization would be a substantial change from the allocation methodologies historically used on the MSU System. As previously discussed throughout this section, the adopted allocation is an attempt to equalize the imbalance of cost on the System with the least disruption possible to the historical operation of the System.

If nuclear investment cost equalization is retained, the Louisiana parties request that we use updated cost data for Grand Gulf 1 and Waterford 3 in applying our methodology. This request previously was made and denied at p. 61,657 of our Opinion. We again decline to use updated cost figures because both the cost estimates and demand projections used in Opinion No. 234 were reasonable when made, and it is necessary to use some fixed point in time in order to provide finality to a proceeding, rather than continuously updating or using spot adjustments.

As in the proceedings below, the parties on rehearing continue to advocate a variety of positions and alternative positions including: accepting the 1982 System Agreement as filed; retaining the 1973 System Agreement's participation unit concept; adopting Judge Head's recommended allocation; adopting full production cost equalization; accepting the Opinion No. 234 allocation; or

[b]OCC and Georgia Gulf Corporation, the LPSC, LP&L and NOPSI.

adopting variations of the above. The majority of proposals have been analyzed either in the initial decisions or in the Opinion, and one fact is clear: none of the proposals is without flaws and none is totally acceptable to any party. At the risk of being repetitive, we believe that Opinion No. 234 results in an allocation scheme that is not at one extreme or the other, but rather represents a balancing of the need to provide an equitable sharing of the investment costs of units that have (or could have) become unforeseeably high due to the unique problems associated with nuclear construction, and the need to recognize the efforts of individual companies on the System and allow them to retain the benefits of units they own to the fullest extent possible.

A final point we wish to emphasize is that the parties have voluntarily agreed to pool resources and share certain costs. They have already voluntarily agreed, under the UPSA in conjunction with the 1982 System Agreement, to allocate Grand Gulf. What our opinion does is to alter in as limited a means as possible the agreed-upon cost scheme, in order to achieve just, reasonable, non-discriminatory and non-preferential rates.

Miscellaneous Rate Issues

Several parties seek rehearing on miscellaneous rate issues in Docket No. ER82-616. MSE seeks rehearing on the issue of rate of return, customer service and sales expenses, use of the UOP and ELG depreciation methods, the annual amount of nuclear decommissioning expense, use of an external sinking fund for accumulating decommissioning amounts, and use of an algebraic tax formula for calculating income tax expense. The LPSC seeks rehearing on the issues of rate of return and cash working capital. AP&L seeks rehearing on use of the UOP depreciation method.

The rehearing arguments raise no matters not previously considered, or that would warrant departure from our decision on the above issues. However, we wish to briefly address MSE's arguments concerning use of the UOP depreciation method. MSE

claims the Commission mistakenly believed that the shakedown period of Grand Gulf 1 was not likely to be more than 12 months, but that the record shows at Tr. 319-20 that the initial shakedown could be two to three years, and might extend up to five years. MSE states that it expects to shut the unit down in mid-May 1986, that it may be shut down for a lengthy period of time, and that the shakedown won't be completed until the unit is restarted. The requirement that MSE request to extend the time for using the UOP method in a future proceeding, at the expiration of 12 months, asserts MSE, creates uncertainty in the eyes of MSE, its and investors and customers, regarding the right to continued use of the UOP method thereafter if shakedown has not been completed.

The transcript pages to which MSE cites contain cross-examination of MSE witness Utley. Mr. Utley states that the stabilization period for Grand Gulf is a range of two to three years, perhaps slightly longer. When asked his basis for stating that the period is two or three years, his reply was:

> Just a personal view, to give you an idea of what I think we're talking about as a stabilizing period. I think circumstances would tell us what that would be. But certainly it's not a period longer than five years, and certainly somewhat shorter than that. Tr.320.

We do not think this testimony provides sufficient certainty as to what length the initial shakedown period will be. Having given MSE the opportunity to come in in future proceedings and seek to extend the time in which to use the UOP method, we also do not accept the argument that there is too much uncertainty in the eyes of MSE's customers and investors. MSE will be allowed to recover its full depreciation expense whether or not the UOP method is used. Furthermore, the UOP method creates more uncertainty for the customers and investors than does the conventional straight-line depreciation method in that it does not assure the company of a fixed annual recovery of depreciation. MSE's rehearing arguments therefore are rejected.

Requests for Recusal

AP&L, the Attorney General of Mississippi, and the MPSC argue that former Commissioner Oliver G. Richard erroneously failed to recuse himself from these proceedings. The Attorney General claims that the recusal decision should have been made by the full Commission or an independent presiding judge and, further, that the wrong legal standard was applied concerning the recusal. We do not find any merit to these arguments, and they are rejected.

Interventions

OCC and Georgia Gulf request that the Commission clarify that it has granted their separate petition to intervene out-of-time, filed March 5, 1985, in the above dockets, and that Georgia Gulf has been admitted as a party intervenor in both proceedings. Mississippi Industries asks the Commission to clarify the Opinion to state that parties to either or both dockets governed by the Opinion may address all issues of fact and law on rehearing or, in the alternative, to grant it leave to intervene out-of-time in Docket No. ER82-616. Jefferson Parish, Louisiana, also asks that we clarify the Opinion so as to remove any doubt that Jefferson Parish was granted late in intervention in each of the above dockets.

We hereby clarify Opinion No. 234 to state that the above parties have been granted intervention in both Docket Nos. ER82-483-000 and ER82-616-000.

The Commission orders:

(A) The requests for rehearing filed in these dockets on July 3, 11, 12, and 15, 1985, are denied.

(B) Opinion No. 234, 31 FERC ¶ 61,305 (1985), is clarified in accordance with this Opinion.

(C) Requests for late intervention are granted in accordance with this Opinion.

(D) The request for rehearing of our denial of a stay of Opinion No. 234 (32 FERC ¶ 61,207 (1985)), filed by AP&L on September 3, 1985 in Docket Nos. ER82-616-028 and ER82-483-024, hereby is denied in accordance with our order denying similar requests for rehearing, issued September 3, 1985, 32 FERC ¶ 61,346.

[THIS PAGE INTENTIONALLY LEFT BLANK]

APPENDIX G

Order Of The Mississippi Supreme Court Denying Rehearing (May 20, 1987)

IN THE SUPREME COURT OF MISSISSIPPI
DECISIONS HANDED DOWN MAY 20, 1987

THE COURT SITTING EN BANC:

* * *

56,762 State of Mississippi, ex rel. Edwin Lloyd Pittman, Attorney General, et al. v. Mississippi Public Service Comm'n, et al.; Petition for Rehearing on March 16, 1987, Order Setting Aside March 13, 1987, Order of Public Service Comm'n Denied. Mississippi Public Service Comm'n Reinvested with Jurisdiction. Petition for Rehearing by Mississippi Power & Light Co. Denied. Petition for Rehearing by Resident Security Holders Denied. Motion of System Energy Resources, Inc. and Middle South Utilities, Inc. to Intervene on Petition for Rehearing and to Shorten Time for Appellants to Respond to Motion Overruled. Motion for Stay of Mandate by Mississippi Power & Light Co. Overruled.

* * *

APPENDIX H

Order Of The
Mississippi Public Service Commission
(May 26, 1987)

BEFORE THE
MISSISSIPPI PUBLIC SERVICE COMMISSION
JACKSON, MISSISSIPPI

U-4620 IN RE: NOTICE BY MISSISSIPPI POWER & LIGHT COMPANY OF ITS INTENTION TO INCREASE RATES APPLICABLE FOR THE RENDITION OF ELECTRIC SERVICE THROUGHOUT ITS SERVICE AREA IN WESTERN MISSISSIPPI; TO BECOME EFFECTIVE ON MARCH 1, 1985

ORDER

Pursuant to the mandate of the Mississippi Supreme Court dated May 22, 1987, in Cause No. 56-762, Mississippi Power & Light Company Rider Schedules MSE-3, MSE-4 (Revised), and RM-3 (Revised) are hereby suspended effective immediately.

Pursuant to the requirements of Section 77-3-39(8) of the Mississippi Code of 1972, as amended Mississippi Power & Light Company is directed to prepare and file with this Commission, within thirty days, an appropriate refunding plan to be completed within ninety days of the date of this Order.

So Ordered this the 26th day of May, 1987.

Chairman Nielsen Cochran votes Aye; Commissioner Lynn Havens votes Aye; Commissioner D. W. Snyder votes Yea.

MISSISSIPPI PUBLIC SERVICE COMMISSION

Nielsen Cochran, Chairman

Lynn Havens, Vice Chairman

D. W. Snyder, Commissioner

ATTEST: A TRUE COPY

Brian J. Ray
Executive Secretary

APPENDIX I
Notice Of Appeal

IN THE SUPREME COURT OF MISSISSIPPI

STATE OF MISSISSIPPI EX REL
EDWIN LLOYD PITTMAN, ATTORNEY
GENERAL, ET AL — APPELLANTS

VS. — NO. 56,762

MISSISSIPPI PUBLIC SERVICE
COMMISSION, ET AL., — APPELLEES

NOTICE OF APPEAL
TO
SUPREME COURT OF THE UNITED STATES
[FILED MAY 20, 1987]

Notice is hereby given that Mississippi Power & Light Company hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Mississippi entered in this action on February 25, 1987, reversing the Final Order on Rehearing entered by the Mississippi Public Service Commission on September 16, 1985, and the decision of the Supreme Court of Mississippi denying rehearing of said final judgment handed down May 20, 1987. This appeal is taken pursuant to 28 U.S.C. § 1257(2).

Respectfully submitted,

MISSISSIPPI POWER & LIGHT COMPANY

BY:____________________
James K. Child, Jr.
Henderson S. Hall, Jr.

ATTORNEYS FOR MISSISSIPPI POWER & LIGHT COMPANY

WISE CARTER CHILD & CARAWAY
PROFESSIONAL ASSOCIATION
600 Heritage Building
401 East Capitol Street
Jackson, Mississippi 39201
(601) 354-2385

Of Counsel

MOTION

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court
of Mississippi

MOTION TO DISMISS

Jesse C. Pennington*
Mississippi Legal Services Coalition
Post Office Box 22887
Jackson, Mississippi 39205
(601) 944-0765

Lewis Burke
Central Mississippi Legal Services
Post Office Box 52
Vicksburg, Mississippi 39180
(601) 636-8322

Attorneys for Appellees

* *Counsel of Record*

22 PH

QUESTION PRESENTED

Whether the decision of the Supreme Court of Mississippi requiring the Mississippi Public Service Commission, in setting retail rates, to inquire into the prudency of Mississippi Power & Light Company's purchasing power under a Federal Energy Regulatory Commission (FERC) approved rate, given other purchase options available to the utility, is preempted by the Federal Power Act's delegation of authority to FERC.

TABLE OF CONTENTS

Page(s)

Cases

NO. 86-1970

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1987

MISSISSIPPI POWER &
LIGHT COMPANY,

Appellant

VS.

STATE OF MISSISSIPPI,
ex rel. EDWIN LLOYD
PITTMAN, Attorney
General, and THE
MISSISSIPPI LEGAL
SERVICES COALITION,

Appellees

On Appeal from the Supreme Court
of Mississippi

MOTION TO DISMISS

Pursuant to Rule 16(b) and (d) of this Court, Appellees move that this appeal be dismissed.

JURISDICTION

This is an appeal from a decision of the Mississippi Supreme Court, entered on February 25, 1987. Appellant's Petition for Rehearing was denied on May 20, 1987. Appellant's Notice of Appeal to this Court was filed May 20, 1987. Appellant seeks review of the result below under 28 U.S.C. §1257(2).

STATUTES AND ORDERS INVOLVED

The statutes involved (Miss. Code Ann., §§77-3-37, 77-3-9) are reproduced in the Appendix to the Jurisdictional Statement, pp. 69(a)-71(a). The administrative Orders and Jurisdictional Opinions involved are reproduced in the Appendix to the Jurisdictional Statement, pp. A-1(a) - H-199(a), §§824(a)&(b) are set out in the Appendix to the Jurisdictional Statement, pp. 61(a)-63(a).

STATEMENT OF FACTS

This case involves an appeal of a decision of the Mississippi Supreme Court issued on February 25, 1987, reversing an Order of the Mississippi Public Service Commission (MPSC). State of Mississippi, ex rel. Edwin Lloyd Pittman, Attorney General, et al., v. Mississippi Public Service Commission, et al., No. 56,762 (Miss. Supreme Court, February, 1987), (One Justice Dissenting) which granted Mississippi Power & Light Company (MP&L) a $326,547.00 rate increase based on a 33% cost allocation of the Grand Gulf Nuclear Plant as approved by the Federal Energy Regulatory Commission (FERC). The MPSC Order was reversed by the Supreme Court of Mississippi for its failure to comply with its statutory mandate (Miss. Code Ann. §77-3-39) to inquire into the prudency of the Grand Gulf investment

before enacting retail rates. The Mississippi Supreme Court held:

> "We do not interpret the law to require that we approve the blind pass-through of a $326 million rate increase to Mississippians without a prudency review; to do so would be a gross abdication of the responsibility of State regulators." State of Mississippi v. Miss. Public Service Commission, supra, at p. 14.

MP&L is a subsidiary of Middle South Utilities, Inc. (MSU), which provides electric utility service within the State of Mississippi. MSU consists of four operating companies: Arkansas Power & Light (AP&L), Louisiana Power & Light (LP&L), Mississippi Power & Light (MP&L), and New Orleans Public Service, Inc. (NOPSI). The MSU system also owns two service companies: Middle South Service, Inc. (MSS) and System Energy Resources, Inc. (SERI). In 1982, the operating companies entered into a Unit Purchase

Sales Agreement (UPSA) for allocation of the cost of the Grand Gulf Nuclear Plant among the operating Companies. The UPSA was filed with FERC and, on June 13, 1985, FERC issued Opinion No. 234, Middle South Energy, Inc., 31 FERC, para. 61,305 (1985), allocating the capacity and energy from Grand Gulf at wholesale rates among the operating companies on the MSU system. FERC allocated 33% of that cost of energy and capacity to MP&L.

On June 24, 1987, the United States Court of Appeals for the District of Columbia Circuit reversed[1/] the decision of FERC[2/] to allocate the Grand Gulf nuclear plant in a manner intended to

---

[1/] Mississippi Industries v. FERC, No. 85-1611, slip op. no. 2 (D.C. Cir. June 24, 1987).

[2/] Middle South Energy, Inc., Op. No. 234, 31 FERC, para. 61,305, reh. denied, Op. No. 234-A, 32 FERC, para. 61,425 (1985).

"equalize" the capacity costs among the four MSU operating companies. The Court remanded the case to FERC with instructions to reconsider the decision to equalize nuclear capacity costs, and vacated the portion of its January 6, 1987 decision[3] where it had affirmed the Commission's rejection of a proportionate allocation of Grand Gulf.

Mississippi State Proceeding

On September 16, 1985, the MPSC granted MP&L a $326 million rate increase to cover its share of the cost of Grand Gulf.[4] MP&L passed these wholesale costs to its retail customers in Mississippi without being required to demonstrate, and the Mississippi Public Service

---

[3] Mississippi Industries v. FERC, 808 F.2d 1525 (D.C. 1987).

[4] Opinion of the Public Service Commission of the State of Mississippi (App. Jurisdictional Statement, B25(a).

Commission had to find, that the expenses were just, reasonable and prudently incurred. Mississippi Public Service Commission v. Miss. Power Co., 429 So.2d 883 (Miss. 1983). The Mississippi Public Service Commission made no such finding but rather passed the entire wholesale share of the Grand Gulf generating plant to the retail customers. The Mississippi Supreme Court reversed the Mississippi Public Service Commission and remanded the case to the MPSC to determine what, if any, of the Grand Gulf related expenses were reasonable and prudent. State of Mississippi v. MPSC, supra, p. 22.

DISCUSSION

MP&L contends that the decision of the Mississippi Supreme Court invaded the federally preempted jurisdiction of the FERC to set wholesale rates for electricity purchased by one subsidiary from

another in interstate commerce.

Nantahala Power & Light Co. v. Thornburg, ___U.S.___, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986).

MLSC respectfully disagrees with the expansive view advanced by MP&L of the scope of the exclusive federal jurisdiction of FERC over the activities of the Mississippi Public Service Commission. MLSC takes the position that a prudency review of MP&L for the purposes of setting just and reasonable intrastate retail rates is a valid exercise of its authority. The Mississippi Supreme Court's Decision was drawn to effectuate no interference of the Federal Regulatory Scheme of FERC's jurisdiction to set interstate wholesale rates.

> "We are aware of the effect that wholesale rates have on retail rates, and we do not challenge the FERC's jurisdiction over interstate wholesale rates." State of Mississippi,

> ex rel. Edwin Lloyd Pittman, et al. v. Mississippi Public Service Commission, et al., No. 56,762 (Feb. 27, 1987) at p. 15.

Important factual distinctions exist between this case and Nantahala. In Nantahala, no question was raised about the prudency or necessity of acquiring low-cost hydro-electric power. The Mississippi Supreme Court recognized this, in their Opinion, citing Nantahala:

> "Without deciding this issue, we may assume that a particular quantity of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, price.

____U.S.____, at ____, 106 S.Ct. at 2360, 90 L.Ed.2d at 958.

The plenary authority of FERC over interstate rates do not invalidate the statutory authority of the Mississippi Public Service Commission from

exercising its

> "...traditional responsibility in the field of regulating electric utilities for determining questions of need, reliability, cost, and other related state concerns." Pacific Gas and Electric Company v. State Energy Resources Conservation and Development Commission, 103 S.Ct. 1713 (1983).

Accordingly, proper consideration should be given to the question of excess capacity and its impact on revenue requirements in the setting of rates. In the instant case, these important issues were not addressed by FERC or MPSC. MPSC made no findings concerning the excess capacity owned by MP&L which exceeded a level for which the retail ratepayers could be reasonably expected to pay; nor did MPSC make any determination that alternative sources of lower-cost energy might be available to MP&L ratepayers.

The Mississippi Supreme Court was strongly convinced that in this case a

prudency review of the Grand Gulf allocation was especially warranted in light of the fact that lower cost power was available by plants owned by MP&L.

> "The record indicates that MP&L still serves 61% of its electrical generating needs from oil and gas units, and, with the purchase of coal-generated energy from ISES 2, the Company is at 85% over peak demand." State of Mississippi v. MPSC, supra, at 15.

This Court in Jersey Central Power & Light Company v. FPC, 319 U.S. 61 (1943) held that the "primary purpose" of the 1935 amendments to the FPA was to give the Federal Power Commission (FPC) authority over sales across state lines which had been held to be beyond state control in Public Utilities Commission v. Attleboro Steam and Electric Co., 273 U.S. 83 (1927). In 1945 the Court stated that the Act showed a "...constant purpose to protect rather than to supervise authority of the

states." Connecticut Light & Power Co. v. FPC, 324 U.S. 515, 525 (1945).

Therefore, under the Federal Power Act, 16 U.S.C. §824(a), Congress created a complementary regulatory framework wherein the states lost no authority as a result of the Act and the federal role filled the gap in state regulation which had been created by the Attleboro case. FERC's jurisdiction does not negate the jurisdiction of the states over the same facilities to, inter alia, approve their construction, establish and allocate their value in rate base, evaluate their operation and maintenance expenses and establish retail rates to recover reasonably incurred costs, access their books and records. Quite simply, a dual regulatory system was created by Congress in 1935 and has existed for over fifty years. FERC was

given the authority to set wholesale rates for interstate sale and transmission of electricity, but otherwise the power of the states was unaffected. A review of the exemption contained in the Federal Power Act is very specific, as is shown in the relevant clause:

> Federal Power Act, 16 U.S.C. §824(a) - "It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of... that part of such business which consists of the transmission of electric energy in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." (Emphasis added)

The Supreme Court of Mississippi made no findings on the federal question presented for review but made an independent decision resting on State law.

> Miss. Code Ann. Section 77-3-39 (1972) which authorizes the MPSC to establish just and reasonable rates which lead to a fair rate of return for the utility. As we have often held, "A fair rate is one which, under prudent and economical management, is just and reasonable to both the public and the utility." Miss. Public Service Commission v. Miss. Power Co., 429 So.2d 883 (Miss. 1983), (citing Southern Bell Tel. & Tel. Co. v. Mississippi Public Service Comm'n., 237 Miss. 157, 241, 113 So.2d 622, 656 (1959) [emphasis added.] State of Mississippi, Slip Op. 13.

In support of its holdings that a prudency review is not precluded by federal law, Mississippi relied on the holding in Appeal of Sinclair Machine Products, Inc., 498 A.2d 696 (N.H. 1985):

> "The approach of this modern trend, which we here adopt and approve as being consistent with preemption doctrine applicable to State regulation of retail electric rates, is to examine whose matters actually determined, whether expressly or impliedly, by the FERC. As to those matters not resolved by the FERC, State regulation is not preempted provided that State regulation would not contradict or

> undermine FERC determinations and federal interests, or impose inconsistent obligations on the utility companies involved."

Id. at 704.

This case is fundamentally different from Nantahala, in that TVA was the only source of power available to Nantahala, and Tapoco, both of which were wholly owned subsidiaries of Alcoa. This Court held that when the North Carolina Utilities Commission changed their entitlement power they altered the FERC-approved allocation in violation of the Supremacy Clause.

Although MP&L is not a "stand alone" company, it owns its own power plant located within MPSC's territorial jurisdiction. In addition, MP&L has partial ownership of a coal generating plant in Arkansas. Nantahala did not compel State utility regulatory Commissions to impose as retail rates any quantity of

energy and capacity approved by FERC, but held that retail rates need not necessarily be increased in direct proportion to the wholesale rates set by FERC. State Regulatory Commissions are not prohibited from taking into consideration, cost-savings in other areas in setting retail rates. Nantahala v. Thornburg, supra, 90 L.Ed.2d at 958.

CONCLUSION

Appellees move to dismiss this appeal on the grounds that, based upon the facts determined below, it was correctly decided and, that appellants present no substantial federal question. As a result, this appeal should not be favorably treated alternatively as a Petition for Writ of Certiorari, and that a Writ of Certiorari should not issue.

Respectfully submitted,

JESSE C. PENNINGTON*
Mississippi Legal Services Coalition
Post Office Box 22887
Jackson, MS 39205
(601) 944-0765

LEWIS BURKE
Central Ms. Legal Services
Post Office Box 52
Vicksburg, MS 39180
(601) 636-8322

*Counsel of Record

August 8, 1987

MOTION

No. 86-1970 (1)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI EX REL.
EDWIN LLOYD PITTMAN, ATTORNEY GENERAL
OF MISSISSIPPI, AND
MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

MOTION OF STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, TO DISMISS APPEAL FILED BY MISSISSIPPI POWER & LIGHT COMPANY

Edwin Lloyd Pittman
Attorney General
State of Mississippi

Frank Spencer
Assistant Attorney General
W. Glenn Watts
Special Assistant Attorney General
P.O. Box 220
Jackson Mississippi 39205

*John L. Maxey II
Cupit & Maxey
304 North Congress St.
P.O. Box 22666
Jackson, Mississippi 39205

*Counsel of Record

CASILLAS PRESS INC. – 1717 K STREET NW WASHINGTON DC 20036 – 223-1220

35pp.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI EX REL.
EDWIN LLOYD PITTMAN, ATTORNEY GENERAL
OF MISSISSIPPI, AND
MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

MOTION OF STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, TO DISMISS APPEAL FILED BY MISSISSIPPI POWER & LIGHT COMPANY

STATEMENT

A. PRIOR STATE PROCEEDINGS

Middle South Utilities, Inc. (MSU), is a publicly traded holding company subject to the Public Utility Holding Company Act. It is the sole owner of the common stock of four subsidiary operating companies, Arkansas Power & Light Company (AP&L), Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (MP&L) and New Orleans Public Service, Inc. (NOPSI).

These companies operate within the States of Louisiana, Mississippi, Arkansas and a very small portion of Missouri. MSU also owns the common stock of System Energy Resources, Inc. (SERI), formerly Middle South Energy, Inc. (MSE), a company established in 1973 to own and operate a proposed new nuclear generating plant, the Grand Gulf Nuclear Electric Station (Grand Gulf) in Port Gibson, Mississippi.

In 1973, appellant MP&L and its sister affiliate MSE applied to the Mississippi Public Service Commission (MPSC) for a certificate of public convenience and necessity (Certificate) to construct the two-unit Grand Gulf plant. The units were projected to cost a total of $1.227 Billion and have a total capacity of 2,500 megawatts. The first unit was scheduled for completion in 1979 and the second unit in 1981.

In the Joint Petition Supp. App. 1-20,[1] MP&L and MSE acknowledged that the proposed construction, ownership and operation of the Grand Gulf project fell under the purview of Mississippi law, specifically the Public Utilities Act of 1956, §73-3-1, *et seq., Mississippi Code of 1972*. Supp. App. 2.

The Joint Petition also set forth the manner in which the MSU System proposed to construct and operate Grand Gulf. It pointed out that the entire MSU System had been planned, constructed, and operated on a system-wide basis. Although various MSU operating companies historically had been assigned individual responsibility to construct new generating units, the planning, location and size of the new units had been made by the System to

[1] In this brief, references to the Appendix To The Jurisdictional Statement of the appellant are cited "App.____."; references to the Supplemental Appendix are cited as "Supp. App.____."

achieve economies for the System as a whole. The Joint Petition made clear that Grand Gulf was no exception and that the size of the Grand Gulf units were determined by the projected load growth of the entire MSU System. Since the costs of the Grand Gulf units were to be so expensive (the first unit alone was shown to be 84% of the original cost of the generating capability of the entire system and 148% of MP&L's total capitalization in 1973), MP&L could not support construction of such magnitude. It was therefore necessary that the MSU System create MSE to facilitate financing and to construct the plant. Supp. App. 5-8.

Since Grand Gulf was to be constructed as a base load unit for the system as a whole, the Joint Petition specified that the capacity and energy from the plant would be divided among the operating companies pursuant to the System Agreement on file with the Federal Power Commission, the predecessor agency to the Federal Energy Regulatory Commission. The System Agreement, among other matters, provided the methodology for the equalization of the costs of capacity in excess of a company's proportionate share among the MSU operating companies.

The MPSC subsequently issued its Order on May 29, 1974, granting the Certificate which authorized the construction of the Grand Gulf plant. Supp. App. 21-40. The Order specifically recited many provisions of the Joint Petition including the method of operation of the System Agreement. The Order also recited the representations made in the testimony of MSU chief financial officer, Donald J. Winfield, MSU Vice President of Finance, that at the appropriate time the System Agreement would be amended to make MSE a party to the Agreement. Supp. App. 33.

Pursuant to the Certificate granted by the Mississippi Commission, MP&L as the MSE contract agent began construction of the plant in 1974.

Construction delays postponed completion of the first unit of Grand Gulf such that the unit was still uncompleted in 1981. In that year MP&L again approached the MPSC for permission to acquire additional capacity. This time the Company's requested acquisition was a 25% ownership interest in the coal-fired Independence plants in Arkansas.

Due to heightened public awareness and concern over the escalating costs of nuclear power plant construction, MP&L was questioned by state officials in public hearings regarding the need for such additional capacity in light of the purported imminent operational startup of the Grand Gulf plant. Additionally, MP&L officials were confronted with a previously undisclosed agreement between the operating companies styled "Memo of Understanding" dated July 10, 1980, which allocated 31.63% of Grand Gulf Unit 1 and 43.97% of Unit II to MP&L.[2] That allocation methodology was totally at odds with the System methodology originally represented to the MPSC.

Company officials in response to the cross-examination testified that the fuel savings to be realized from the coal fired generating plants would more than offset the costs of the additional plant acquisitions. Further, MP&L President Donald Lutken reassured the MPSC as to the extent of its jurisdiction over Grand Gulf and its ability to control costs of electricity to its ratepayers. Mr. Lutken testified in response to the direct question from Counsel for the Attorney General:

---

[2] These percentages represent MP&L's proposed ownership of MSE's 90% share of the Grand Gulf.

> Q. [Question by Mr. Spencer] Is this latest Memo of Understanding regarding the allocation of capability down at Grand Gulf. . .?
>
> A. [Answer by Mr. Lutken] Yes, sir.
>
> Q. [Question by Mr. Spencer] Will the purchases of energy from Grand Gulf *require the approval of the Mississippi Public Service Commission?* (Emphasis supplied.)
>
> A. [Answer by Mr. Lutken] Yes, sir. Supp. App. 48.

Later in the hearings Mr. Lutken testified to the same effect:

> . . .we can make these decisions but what I think we're trying to say is *this Commission has the final say-so as to what goes into MP&L's rate base, whether it be 19% of Grand Gulf or 33% of it.* (Emphasis supplied). Supp. App. 50.

Based on MP&L's assurances, the MPSC granted the Certificate for the purchase of the additional 370mw of capacity from the Independence plants on June 19, 1981.

B. PROCEEDINGS BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION.

In 1982, the MSU System filed two contracts with the Federal Energy Regulatory Commission (FERC) for approval. The first was styled the Unit Power Sales Agreement (UPSA). It was filed by MSE and contained an allocation of Grand Gulf based on the earlier Memo of Understanding executed by the MSU operating companies. That case was docketed by FERC as ER82-616-000. The second case was filed by the service company subsidiary for the MSU System, Middle South Services, Inc. (MSS) and was docketed by the FERC as

ER82-483-000. That case involved several changes to the 1973 System Agreement, the most significant of which was to change the method of equalizing capacity costs on the MSU system. The method of allocation of Grand Gulf to the various jurisdictions became the central issue in both cases. Appellees State of Mississippi (Attorney General) and Missisippi Legal Services Coalition (Coalition) intervened in both cases.

In the MSE case, reported at 26 FERC ¶63,044, which was heard first, Administrative Law Judge Ernst Liebman found the as-filed UPSA:

> . . . perpetuates, rather than rectifies, the discrimination caused by the timing of the construction of the nuclear units, based upon decisions reached by the MSU system to the serious detriment of MSU's Louisiana and Mississippi ratepayers, who would pay about four times more for nuclear capacity as MSU's Arkansas ratepayers and substantially more in overall rates.

26 FERC at p. 65,107.

To rectify the discrimination found, Administrative Law Judge Liebman decided the appropriate remedy was to equalize all nuclear generating capacity costs among the MSU operating companies. Illogically, the decision proposed an increase in MP&L's allocation of Grand Gulf from 31.63% to 33% of the plant.

In the MSS case reported at 30 FERC ¶63,030, Administrative Law Judge Daniel Head examined the Grand Gulf allocation in the context of the operation of the entire MSU system and the proposed new System Agreement. Administrative Law Judge Head decided that the method of creation and the proposed operation of Grand Gulf was an anomaly among generating plants on the MSU system.

Therefore he found it appropriate that the expensive plant be divided among the MSU operating companies based upon their average annual energy demand (or total energy usage) on the MSU system. The effect of Administrative Law Judge Head's initial decision was a recommended allocation of approximately 15% of the capacity and energy of Grand Gulf to MP&L.

After receiving briefs on exceptions from the numerous parties in both cases, the FERC issued its consolidated order on June 13, 1985, resolving the issues in both cases. *See,* 31 FERC ¶61,305. After granting rehearing, FERC clarified its order on September 26, 1985. *See,* 32 FERC ¶61,425. FERC adopted Administrative Law Judge Liebman's decision allocating 33% of Grand Gulf to Mississippi as well as approving the new system methodology of equalizing excess capacity costs. Sixteen parties before the FERC noticed appeals to the Circuit Courts of Appeal.

C. MISSISSIPPI RATE PROCEEDINGS

MP&L filed with the MPSC for a rate increase on November 16, 1984, seeking an increase in rates to cover increased costs of operation due to several factors including inflation, the operational startup of Unit 2 of the Independence Steam Electric Station and also the costs associated with MP&L's share of Grand Gulf.

In regard to the revenues requested related to Grand Gulf, MP&L filed two different proposals with the MPSC. The first proposal was a rate moderation plan designed to recover revenues for MP&L based on an allocation of 19% of the costs of Grand Gulf. The figure of 19% represented the percentage of Grand Gulf that at least one commissioner felt was originally represented to him as MP&L's share of Grand Gulf. The second proposal

was a rate moderation plan designed to recover revenues for MP&L based on an allocation of 33% of Grand Gulf. The 33% figure was derived from the initial decision of Administrative Law Judge Liebman of FERC.

The initial action of the MPSC was to approve an interim rate increase on January 17, 1985, of approximately $45 Million which gave MP&L immediate revenues to compensate for its "non-Grand Gulf" revenue deficiency. Then on March 5, 1985, the MPSC, upon its own initiative, severed from the rate case the issues of the prudency of MP&L's capacity purchases, excess capacity and the design of the rates necessary to recover any further revenue deficiency.

Pursuant to state law, the various parties to the rate cases assembled for a prehearing conference to determine if any of the issues in the case could be resolved without further litigation. As a result of discussions held over several days, the parties were able to forward to the MPSC a stipulation that MP&L was entitled to a permanent $48.6 Million increase in its rates for "non-Grand Gulf" expense items. Expressly excluded from the stipulation were the issues of the prudency of MP&L's capacity additions and the revenues to cover MP&L's share of Grand Gulf.

After abbreviated public hearings on the case, the MPSC issued its order in the case on June 14, 1985, one day after FERC had issued its initial decision. The MPSC granted the stipulated $48.6 Million increase; however, it granted no rate increase to MP&L for its costs associated with Grand Gulf.

On June 27, 1985, MP&L filed a request for rehearing with the MPSC citing the FERC decision that MP&L was allocated 33% of the capacity and energy costs of Grand Gulf. The MPSC granted the rehearing but did not sche-

dule a rehearing date. Consequently on July 26, 1985, MP&L filed an application for emergency rate relief. Emergency hearings were held on August 12 and 13th, 1985. Prior to the MPSC issuing its order, MP&L filed suit against the MPSC on August 21, 1985 in Federal District Court. The MPSC then issued its order denying MP&L's emergency rate relief on August 23, 1985. Before MP&L's federal action could be argued, the MPSC set the rehearing for September 9, 1985. After rehearing the case on September 9 and 10, 1985, the MPSC issued its "Final Order on Rehearing" on September 16, 1985, which allowed MP&L to collect rates for 33% of Grand Gulf through a ten-year rate moderation plan.

The Attorney General and the Coalition subsequently appealed the MPSC Order directly to the Mississippi Supreme Court as provided for by Mississippi law. The primary errors alleged were:

1. The setting of final rates without the possibility of refunds after severing the acknowledged issue of the prudency of MP&L's capacity additions;

2. Substantive *ex parte* communications during the case between the MPSC and MP&L on the merits of the case;

3. The adoption of a rate moderation plan without the support of substantial evidence in the record of the terms of the plan and its future impact on the service area, and

4. That MP&L should be estopped from seeking rates related to a Grand Gulf allocation greater than that originally represented to the State in order to obtain authorization for construction.

After briefing and lengthy oral argument on the case, the Mississippi Court on February 25, 1987, found merit in the arguments of the appellees that the MPSC had erred in awarding final rates without considering the prudency of MP&L's capacity additions. After the Mississippi Court denied MP&L's request for rehearing on May 20, 1987, the Company noticed appeal to this Court on the same date.

D. PROCEEDINGS BEFORE THE CIRCUIT COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA.

Prior to the decision of the Mississippi Supreme Court, the appeals of the various parties to the FERC decision were consolidated before the Circuit Court of Appeals for the District of Columbia in Cause No.85-1611, *Mississippi Industries v. FERC.*

On January 6, 1987, that Court affirmed the FERC order in its entirety; however, Circuit Judge Robert Bork dissented as to the FERC methodology utilized to allocate nuclear investment costs including the Grand Gulf plant, terming it "not rational."

The Attorney General, MPSC, MP&L and two other parties, Mississippi Industries and the City of New Orleans, subsequently sought rehearing *en banc* of the Court based on the dissent. On April 3, 1987, the full Court granted rehearing and set up a briefing schedule. Subsequently, after these parties had filed their initial briefs but prior to receipt of the response by FERC, the original panel reconsidered its decision, reversed the FERC for the reasons originally stated in the dissent and remanded the case to FERC for reexamination of the decision of the agency on the methodology of equalizing nuclear capacity investment costs among the MSU operating companies. *Mississippi Industries v. FERC,* No. 85-1611 (D.C. Cir. June 24, 1987).

ARGUMENT

A. THIS APPEAL SHOULD BE DISMISSED FOR LACK OF JURISDICTION.

Appellant appeals from an order which lacks finalilty under 28 U.S.C. §1257. The Mississippi Supreme Court reviewed the record from the Mississippi Public Service Commission to determine if that administrative agency had complied with its statutory and caselaw duties to assure that MP&L had met its burden of proof to establish that the proposed rates would be just, reasonable and prudently incurred. The State Court concluded that the PSC had plainly failed to make such a determination. The Mississippi Supreme Court remanded the case to the MPSC for further proceedings so that it could comply with state law. Until the State Court has finally adjudicated any federal issues present in this case, review by this Court is precluded. *Radio Station WOW, Inc. v. Johnson,* 326 U.S. 120, 124 (1945).

The record before the MPSC reflected that without any energy from Grand Gulf, MP&L was 85% over peak demand. App. 15a. The State Court concluded: "Since Mississippi cannot use 33% of Grand Gulf's power, the 1982 System Agreement providing for the allocation of 33% of its cost would *seem* to be imprudent." (Emphasis added) App. 16a. The availability of lower cost energy and the most economical and efficient mix of that energy for retail rate purposes are questions properly presented to and determined by the MPSC. Such proceedings are required by state law. *Miss. Code Ann.,* §77-3-39 (1972); *Mississippi Public Service Commission v. Mississippi Power Company,* 429 So.2d 883 (Miss. 1983); *Southern Bell Tel. & Tel. Co. v. Mississippi Public Service Co.,* 237 Miss. 157, 113 So.2d 622 (1959). As a matter of state law, these ques-

tions are preserved for the states to decide. *Nantahala Power & Light Co. v. Thornberg*, ___ U.S. ___, 106 S.Ct. 2349, 90 L.Ed.2d 943,955 (1986). The FERC, contrary to the brief filed by its attorneys, recognizes the traditional role of states in the regulatory process. *Middle South Services, Inc.*, 32 FERC at 61,953; App.172a; *Philadelphia Electric Co.*, 15 FERC ¶61,264 (1981).

The State Court thus returned the case to the MPSC, relying on the expertise of that agency to determine, among other things, whether MP&L had demonstrated prudent and economical management in its mix of costs of the energy to be paid for by the retail ratepayers, in light of the availability of lower cost energy from alternative sources. 506 So.2d 978,987 (Miss. 1987); App. 18a-19a. The State Court did not decide the issue, but held that the MPSC had the authority as well as the obligation to make the decision. On this point, this Court and the Mississippi Supreme Court are in agreement:

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though the higher cost power actually purchased is obtained at a FERC-approved, and therefore, reasonable *price*. *(Emphasis in original)*

Nantahala, 90 L.Ed.2d at 958.

The elements of retail ratemaking require the MPSC to examine every expense chargeable as rates to the consumer to determine if that expense was incurred as a result of prudent or economical management. In his treatise on public utility regulation, A.J.G. Priest discussed the treatment of operating expenses as an element of ratemaking.

> Regulatory agencies may exclude particular outlays from operating expenses (1) if the questioned outlays represent "inefficiency" or "improvidence," or (2) managerial discretion has been abused or (3) the action taken has been "arbitrary," or "inimical to the public interest," or (4) there has been "economic waste," or (5) such outlays were not legitimate operating expenses because they were "in excess of just and reasonable charges." Any denial of the right to include actual outlays and operating expenses must be based upon competent evidence. Utility managements may not be arbitrary and capricious and neither may regulators.

1 A. Priest, *Principles of Public Utility Regulation*, 51 (1969).

While it is apparent that MP&L seeks an appeal from an order which lacks the requisite finality as a matter of state administrative law requirements, this Court can examine the question presented to determine if it falls within one of the four exceptions carved out by earlier decisions. *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 477 (1975).

On remand, the State Court did not limit the MPSC in the exercise of its administrative responsibilities. On further proceedings, the MPSC can, upon adequate proof, determine that the purchase of the total costs associated with Grand Gulf were just, reasonable and prudently incurred and could be charged in retail rates. The proof might well show and the MPSC could then conclude that MP&L had available to it adequate supplies of lower cost electricity and that some amount of the energy from Grand Gulf, less than the total amount owned by MP&L, would be included in the retail rates. The MPSC may also determine that from the panoply of expenses incurred by

MP&L, there are areas which, when combined with the Grand Gulf costs, result in a reduction of the impact of the higher nuclear costs. *Nantahala, supra,* 90 L.Ed.2d at 955; *Narragansett Electric Company v. Burke,* 119 R.I. 559, 381 A.2d 1358 (1977). Compliance with the state law and fundamentals of proper ratemaking by the MPSC would in none of the foregoing alternatives draw into question the cost of energy and capacity for Grand Gulf as set by the FERC. The decision to remand to the MPSC is not conclusive nor is the outcome of further proceedings preordained. *Cox Broadcasting Corp., supra,* 420 U.S. at 479. This exception does not apply.

Among the decisions which the MPSC can make in this case and which would be subject to review by the State Court, the issue raised by appellants here will be preserved. *Radio Station WOW, supra,* 326 U.S. at 127. There is no conceivable way that the PSC could separate from its considerations the Grand Gulf energy and capacity allocated by the FERC to MP&L for that is the principal reason for the rate increase sought by MP&L. As previously stated, there are dispositions which would "make unnecessary decision on the federal question." *Cox, supra,* 420 U.S. at 480. The question, therefore, does not fall within the second category of exceptions to the finality requirement.

The third exception to the finality requirement described in *North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc.,* 414 U.S. 156 (1973) distinguishes itself from the facts of this case. There, the state supreme court had declared unconstitutional a state statute but had remanded the case to the administrative agency for determination of the remaining state law issues. This Court exercised jurisdiction because the federal issue would not

survive on remand regardless of the result of the state administrative proceeding. That exception does not apply here where the bright line between federal and state jurisdiction is ever present. Any invasion by the state into the preempted area of wholesale ratemaking and interstate commerce would be well preserved for review by this Court.

The fourth category of exceptions to the finality requirement includes those cases where the continued vitality of the ruling of the state court would erode federal policy notwithstanding the prospects of further proceedings in state court. This exception relates to cases involving exclusive federal jurisdiction of the cause of action or a special federal statute. *Construction Laborers v. Curry,* 371 U.S. 542 (1963). Federal jurisdiction is not exclusive in this system of dual regulation.[3] There is no special federal statute governing prudency determinations in the purchase of wholesale electric power. Therefore, this case does not fall within the exception.

Mississippi should be given the opportunity to complete the process leading to the adoption of retail rates which comply with state law, yet observe federal requirements. That process is not complete at this time. Yet, appellant would have this Court draw a bright line between the jurisdictions of the FERC and the MPSC at this premature stage. This Court has long ago done this with the wholesale/retail distinction. It should now permit the MPSC to proceed with its responsibilities. Only then, if the question

---

[3] In fact, the Federal Power Act was adopted to fill the gap left when the states were limited to the regulation of intrastate retail rates. *Public Utilities Commission v. Attleboro Steam & Electric Co.,* 273 U.S. 83 (1927).

is presented, should this Court determine if it should address it.

Appellant relies on *Nantahala* III to support is request for jurisdiction. That order simply returned the case to the North Carolina Supreme Court to carry out the decision of this Court. As this Court held in *Nantahala,* any decision by the North Carolina Utilities Commission which changed the relative quantities of entitlement energy and purchase power of necessity would change the FERC approved mix of the different price energy, hence invade the FERC jurisdiction. The further proceedings of the North Carolina Utilities Commission could not change that. *Nantahala, supra,* 90 L.Ed.2d at 958. As described herein this case does not fall within that exception since there are multiple alternative sources of energy which were not available to Nantahala but which are available to MP&L and which may bear on the MPSC's further considerations.

B. THE QUESTION PRESENTED IS NOT SUBSTANTIAL.

Appellant seeks to circumvent the authority vested in Mississippi to determine its own need for electrical generating facilities. The FERC cannot in any event preempt the authority of the states to determine that need. 16 U.S.C. §824 (1978), *Pacific Gas & Elec. v. Energy Resources Comm'n,* 461 U.S. 190, 212 (1983). Appellant would have all wholesale rate decisions by the FERC act as a bar to the states from consideration of issues of excess capacity and the availability of lower costs energy, all questions which directly relate to the "economic question of whether a particular plant should be built." *Id.* at 207. That which the Constitution prohibits directly, cannot be accomplished indirectly.

It is of particular importance that the FERC did not address the issue of prudency of the purchase of power from Grand Gulf for retail ratemaking purposes. Adoption of the Federal Power Act established a system of dual regulation of electric power. Consideration of prudency by each jurisdictional level of regulation for its own purposes is consistent rather than inimical to Congressional intent.[4]

To contend as appellant does that the FERC has decided all prudency issues raised by the Mississippi Supreme Court is to ignore both the actual proceedings of the FERC in the Grand Gulf matter and the role that the FERC has itself described. The Administrative Law Judge specifically excluded consideration of prudency at the retail level.

> PRESIDING JUDGE:
> And I don't think I have to get into the prudency question on that issue because my statutory standards, as I understand them, are what the rates that are finally prescribed by the Commission, initially by me, are just and reasonable and nondiscriminatory.

FERC, Docket No. ER-616-000, Tr. 166, Supp. App. 59-60.

> PRESIDING JUDGE:
> Well, I wouldn't get into what the state would do at the retail level about the amount of power purchased, or whether the price was fair, or anything. I would only make the finding as to justness and reasonableness of the agreement as

[4] In another area of utility regulation, federal and state regulators regulated the same telephone plant, but applied differing methods of depreciation. This Court found that system of dual regulation was permitted. *Louisiana Public Service Comm. v. FCC,* ___ U.S. ___, 106 S.Ct. 1890, 1899 (1986).

finally modified, if at all, by me, and whether or not it is discriminatory. And I would not get into a prudency argument unless one of the Intervenors raises a prudency question.

FERC, Docket No. ER-616-000, Tr. 168. Supp. App. 61.

PRESIDING JUDGE:
I don't think I or the Commission would ever do that, in other words, make a finding saying "Here are our determinations about prudency and they govern retail rates and everything else."

FERC, Docket No. ER-616-000, Tr. 171. Supp. App. 63.

And the Presiding Judge even contemplated that the states would be free to act in all retail matters, including the prudency of the allocation.

PRESIDING JUDGE:
I don't think you can put me in a position or this Commission in a position of deciding a prudency issue on the allocation issue in such a way that no one can possibly raise this in State Court. I think that's the problem you have. I may be wrong.

I don't intend to get into state jurisdiction, but I do intend to get into what a fair and just and reasonable and non-discriminatory rate schedule and agreement is.

MR. EASTLAND:
Wholesale level.

PRESIDING JUDGE:
At the wholesale level. Right.

FERC, Docket No. ER-616-000, Tr. 248. Supp. App. 66.

In the decision of *Philadelphia Electric Co.,* 15 FERC ¶61,264 (1981), the FERC accepted for filing as a rate schedule a contract for the purchase and sale of energy and related capacity but it held that this action did not preclude state agency review of the transaction. The language of the decision points to the statutory limitation which FERC itself recognizes:

> "[W]e wish to make it clear that our decision to accept the contract . . . does not in our view, bind us or the Pennsylvania Public Utility Commission to any particular treatment of these items in the cost of service for the wholesale and retail requirements, customers of [the purchasers].
>
> * * *
>
> [W]e do not mean by this order to prejudge, for our own purposes, or those of the respective state commission, a determination of the prudence of either party entering into this contract.

15 FERC at ¶61,601. See also, *Pennsylvania Power & Light Co.,* 23 FERC ¶61,325 (1983). This was more recently reaffirmed in *American Electric Power Service Corp.,* 32 FERC (CCH) ¶61,363 (1985). See also *Appeal of Sinclair Machine Products, Inc.,* 498 A.2d 696 (N.H. 1985) cited by the Mississippi Supreme Court for the proposition that prudency left unexamined by the FERC is properly reviewable by the states.

The ice on which appellant offers this Court the chance to skate is perilously thin. Its interpretation of the facts in this case and its reliance on various authorities would compel this Court to decide that a state no longer has any role in retail ratemaking once a utility becomes highly coordinated or integrated, or a member of a power pooling arrangement. Appellant can find no support for that position in the Federal Power Act, this Court's own authorities

which adhere to a respect for a bright line between federal and state utility regulatory roles, the role which the FERC has chosen to adopt, or the peculiar facts of this case. Appellant would have this Court believe that once the FERC made its decision in this case, the retail consumers of MP&L and Mississippi would automatically begin paying for 33% of Grand Gulf, whether they needed the energy from Grand Gulf or whether there was lower cost energy available from alternative sources. Thus, there would be no retail ratemaking function to be exercised. This misapprehends the durable concept of dual regulation.

Appellant relies exclusively on *Nantahala* to frame its substantial question. *Nantahala* is self-distinguishing from this case and it should not be relied on for the proposition that FEC approved wholesale rates must be adopted as a federally imposed surcharge by the regulator of retail rates regardless of all state requirements of ratemaking. A comparison of the facts in *Nantahala* with this case is useful.

Nantahala and Tapoco were both wholly owned subsidiaries of Alcoa. Both Nantahala and Tapoco transmitted all of their self-generated power to TVA. In return, through a series of FERC-approved agreements, Nantahala and Tapco received from TVA a mix of low-cost entitlement power while Nantahala bought an additional amount of the high-cost purchase power from TVA. Any change in the mix of purchased power and entitlement power by Nantahala changed the costs of the power to both companies. 90 L.Ed.2d at 947. TVA was the only source of power available to Nantahala. *Id.* at 958.When the North Carolina Utilities Commission (NCUC) attempted to change the mix of entitlement power and purchased power, it necessarily changed the FERC allocated costs. This Court held that the action taken by NCUC violated the Supremacy Clause.

The facts of this case are materially different. MP&L owns its own power located within its territorial jurisdiction as well as partial ownership in the Independence coal generating plant in Arkansas. While MP&L is not a "stand alone" company since it operates through a system arrangement with its sister subsidiaries, its cost of energy and capacity are in direct relationship to its own generation capacity.[5] The FERC decision, in fact, refused to equalize the investment costs of system-wide generation and even failed to equalize all nuclear generation costs, a point still under attack in the appellate process reviewing the FERC order.[6] App. 171a-172a. As the Mississippi Supreme Court observed:

> In this case, there is no doubt that Misssippians do *not* need the power provided by Grand Gulf, and that lower cost power is available elsewhere (in fact by plants owned by MP&L). The record indicates that MP&L still serves 61% of its electrical generating needs from oil and gas units, and, with the purchase of the coal-generated energy from ISES 2, the company is at 85% *over peak demand.* Furthermore, MP&L indicated at oral argument that it is selling the less expensive energy off the system and retaining the electricity allocated to it from Grand Gulf. (Emphasis in original)

App. 15a.

[5] The FERC emphasized the specific nature of its opinion with regard to the degree of integration in the Middle South System: "A reading of the Opinion [234] does not reflect a 'monolithic' entity, but recognize the role of the individual companies in System decisionmaking, and the interplay between System and individual company needs." App. 175a.

[6] Those very issues were the point of the *sua sponte* reversal by the Court of Appeals for the District of Columbia Circuit in *Mississippi Industries v. FERC*, Nos. 85-1611, *et al.* (D.C. Cir. June 24, 1987).

This Court's opinion in *Nantahala* spoke to the striking differences in that case from the set of facts which MP&L presents here.

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*. (Emphasis in original)

90 L.Ed.2d at 958. This statement has been read to this effect by at least one circuit court of appeals. See, *New Orleans Public Service v. City of New Orleans*, 798 F.2d 858, 860 (5th Cir. 1986).[7]

The Mississippi Supreme Court reversed the action of the MPSC because it had adopted certain operating expenses in retail rates without any finding that they were just, reasonable and prudently incurred. In doing so, it did not act in derogation of the FERC or of its own recognition of the bright line between interstate and intrastate ratemaking. *United Gas Corp. v. Mississippi Public Service Commission*, 240 Miss. 405, 1278 So.2d 404 (1961) as adopted in *Narragansett Electric Company v. Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), *cert. den.*, 435 U.S. 972, 978 (1978). This Court and the *Narragansett* doctrine concur in the conclusion that, "An increase in FERC-approved wholesale rates need not lead to an increase in retail rates." *Nantahala* at 955. The appellant, thus, should find little support for its position in *Nantahala*,

[7] This decision has added importance because the Court was considering the impact of this FERC order on New Orleans Public Service, Inc., a sister subsidiary of MP&L within the Middle South System.

since that decision sets forth principles which undergird the correctness of the decision of the Mississippi Supreme Court.

Applicant's argument with regard to the "trapping" of costs fails because of the same factual distinctions in *Nantahala* and this case.[8] Nantahala received all of its power through the FERC-approved arrangement from TVA. Any deviation from the arrangement produced a change in the price of the energy. A reduction in the price paid to Nantahala by its ratepayers resulted in a short-fall from the price it had to pay its wholesale supplier. The costs were thus trapped. *Id.* at 956-7.

MP&L has sources of power other than Grand Gulf, sources it apparently has not seriously considered. Costs vary from each source. Changing the mix will not change the FERC ordered price of Grand Gulf generated energy but will only change the quantity of that energy used by MP&L. As plainly stated, this is not an impermissible exercise of the state's power to set retail rates. *Id.* at 958.

Reliance upon *Appalachian Power Company v. PSC of West Virginia*, 812 F.2d 898 (4th Cir. 1987) belies the appellant's attempt to blur the bright line between wholesale and retail ratemaking. The roles are different.

> Moreover, the issue before the state commission differs from that before FERC. The state commission considers whether the purchasing utility chose wisely among alternative sources of energy

[8] This is a term of convenience used by MP&L to bolster its arguments. It has contradicted its own statements: ". . . MP&L admitted at oral argument that it is selling the less expensive energy off the system and retaining the electricity allocated to it from Grand Gulf." 506 So.2d at 985. Thus, MP&L is deciding by which source of power it wants to be "trapped."

> supply in entering into the particular agreement, not whether the terms of the agreement are just and reasonable.

812 F.2d at 903. The Fourth Circuit recognized the distinction pointed out in the *Nantahala* decision. This Court rejected as inapplicable the *Pike County* line of authority in part because there was only one available source for the particular 'entitlement' energy at issue in *Nantahala*. *Id.*, 90 L.Ed.2d at 958.

Appellant's assertion that MP&L could not have treated itself as subject to an allocation of power supplies at a cost that is different from FERC's interpretation of what would be a fair allocation is incorrect. Jurisdictional Statement, p. 15. MP&L very much unlike Nantahala had multiple sources of energy. App. 8a-9a, 15a. This Court in *Nantahala* went further to say that with respect to the North Carolina utility "no source of power besides entitlement and purchase power from TVA is said to be available to Nantahala." 90 L.Ed.2d at 958.

Appellant asserts that the FERC had "all the power sources from the Middle South System before it." Jurisdictional Statement, p. 14. The FERC did not address or even consider the source or the mix of generating sources available to the individual operating companies nor the pricing of energy and capacity from non-system generating facilities.

FERC noted:

> . . .[G]eneration facilities and retail rate regulation should be left to the states and that cost equalization should be ordered only if necessary to insure the just, reasonable and non-discriminatory agreement governing transactions among the MSU subsidiaries." App. 171a.

> An important point to be emphasized here is that our decision was a limited one . . . [W]e did not order production cost equalization, nor did we order equalization of all nuclear generation costs . . . .

App. 171a. "The basic nature of regulatory control retained by the states under previous System Agreements remains unchanged." App. 172a. The FERC recognized the integrated nature of the Middle South System only to the extent that the subsidiaries spoke as one on the subject of major decisions with regard to the system (particularly as to generation additions being made by and for the system as a whole). App. 175a. Thus, it is pertinent that the decision of the FERC did not preclude contined retail ratemaking by the State of Mississippi but only set the price which its ratepayers must pay for energy generated by Grand Gulf and prudently purchased by MP&L.

C. THE MISSISSIPPI DECISION DID NOT VIOLATE THE COMMERCE CLAUSE.

The decision of the State Court does not violate the Commerce Clause. As stated above, no rates have yet been set by the MPSC so that any determination can be made with regard to the effect on interstate commerce. There can be no doubt that the MPSC can proceed with its retail ratemaking responsibilities by determining from the available sources of power the most prudent and economical mix for the ratepayers in MP&L jurisdiction. Sources of power before the MPSC will include MP&L's native load located in Mississippi, its interest in the Independence Steam Electric Staion located in Arkansas, as well as the power from Grand Gulf, which is located in Mississippi.

Any state ratemaking action will have some influence or some effect upon interstate commerce. These actions do not necessarily interfere with interstate commerce. *Arkansas Elec. Coop. v. Ark. Public Serv. Comm'n.*, 461 U.S. 375, 395 (1983). Contrary to the assertion of appellant, the *Nantahala* decision contemplated the role of the intrastate ratemaking agency to be selective among sources of power.[9]

The authority of *Middle South Energy, Inc. v. Arkansas Public Service Commission*, 772 F.2d 404 (8th Cir. 1985),7 *cert. den.*, 106 S.Ct. 884 (1986) does not apply to this case. The Arkansas Public Service Commission attempted to directly interfere with the authority of the FERC to make allocations of energy for the purpose of setting wholesale rates. Any action of the MPSC in setting retail rates will leave undisturbed the order of the FERC which set wholesale rates of energy dispatched from Grand Gulf.

D. MP&L SHOULD BE EQUITABLY ESTOPPED FROM ARGUING TO THE COURT THAT THE STATE'S ACTIONS IN THIS CASE ARE PREEMPTED.

MP&L does not come to this Court with clean hands and should be estopped from asserting to this Court that the State of Mississippi is preempted by federal law from a

---

[9] Appellant cites *New England Power Company v. New Hampshire*, *supra*, for the proposition that a state may not embargo high cost power. That authority dealt with the constitutionality of a New Hampshire statute requiring that state to reserve its cheaper hydroelectric power for its own use. The Court explicitly did not rule on the question of the impact on interstate commerce should the New Hampshire Public Service Commission compel the utility to enter into contracts which would reflect the lower cost rate of its native hydroelectirc power. 455 U.S. 343, n. 10.

prudency determination of MP&L's participation in the Grand Gulf project.

In the instant case, the State through the MPSC has relied to its detriment throughout the history of the plant on the inaccurate representations of MP&L regarding how Grand Gulf would be allocated and the extent of state jurisdiction over Grand Gulf.

This Court in a recent case repeated the principle of equitable estoppel. In *Heckler v. Community Health Services,* 467 U.S. 51, 81 L.Ed.2d 42, 51; 104 S.Ct. 2218 (1984), the Court stated:

> Estoppel is an equitable doctrine invoked to avoid injustice in particular cases. While a hallmark of the doctrine is its flexible application, certain principles are tolerably clear:
>
> "If one person makes a definite misrepresentation of fact to another person having reason to believe that the other will rely upon it and the other in reasonable reliance upon it does an act . . . the first person is not entitled.
>
> "(b) to regain property or its value that the other acquired by the act, if the other in reliance upon the misrepresentation and before discovery of the truth has so changed his position that it would be unjust to deprive him of that which he thus acquired." Restatement (Second) of Torts §894(1) (1979).

81 L.Ed.2d at 51. See also 3 J. Pomeroy, Equity Jurisprudence §805 p. 192 (S. Symons Ed. 1941).

While it could be accurately argued that the representations made by MP&L and MSE in 1974 to the State through its licensing arm, the MPSC, were not initially misrepresentations, they rapidly acquired that character as

the MSU System secretly began deliberations shortly thereafter to change the methodology of Grand Gulf allocation. See 26 FERC ¶63,044, App. 396a-402a. Even after the MSU operating companies finalized the Memorandum of Understanding on July 10, 1980, an allocation plan totally different from the original MSU representations, almost a year passed before the MPSC was made aware of the new MSU plan. Even then the information regarding the agreement came not from MP&L, but from an intervenor in a July, 1981 hearing on MP&L's request to purchase additional capacity from Independence Coal plant in Arkansas.

Further, when the MP&L chief executive officer was questioned at that hearing regarding the the impact of the Memorandum, he continued to assure the MPSC of that agency's authority to make the ultimate determination as to the costs that must be borne by Mississippi ratepayers.

There can be no doubt that the MPSC acted on these misrepresentations to the State's detriment. The MPSC granted the certificate for Grand Gulf construction in spite of the projected huge construction costs secure that the representations made to it in sworn testimony about how the plant would be allocated would be followed. While the MPSC pursued other duties, the MSU System altered the terms of its Certificate without input from any State. An integral part of the Mississippi Court's decision were the representations made to the State in 1974 to obtain the Certificate.[10] App. 4a-5a.

[10] This equitable estoppel argument was recently accepted by the U.S. District Court for the Southern District of Mississippi when the Sister Company, SERI (formerly MSE), in a related proceeding attempted to deny MPSC jurisdiction over the Company. Supp. App. 41-47. The argument was rejected by FERC Opinion 234 and by the Circuit Court of Appeals with both bodies stating FERC was not bound by proceedings in which it was not a party. These decisions, however, misconstrue the argument and nature of the doctrine; that is, the thrust is not that an adjudicating body can be bound in its judicial capacity by misrepresentations but that equitably, a person should not be allowed to benefit from his misrepresentations to the detriment of one who relied on them.

Even after the secret intra-system negotiations were revealed, Company officials hastened to reassure the MPSC that it had the very jurisdictional authority which MP&L now urges this Court is preempted. There can be no doubt that the State again acted to its detriment, since after these hearings it allowed MP&L to acquire even more capacity. At that time and later, the MPSC refrained from exercising options it may have taken to assure lower capacity costs in utility rates for its citizens.

This Court recognized in *Pacific Gas & Elec. v. Energy Resources Comm., supra,* that Congress has preserved the traditional role of the states in determining the economic questions of whether a particular generating plant should be built. If state commissions are to have the authority to make rational decisions concerning the need for such new generating facilities, they must be able to rely on the representations and testimony made by the utility companies to secure the necessary construction certificates. Equitably, this Court should not now allow MP&L to come before this Court in contravention of its prior representations to the MPSC.

CONCLUSION

The Court should deny probable jurisdiction and dismiss the jurisdictional statement.

Respectfully submitted,

STATE OF MISSISSIPPI, EX REL.
EDWIN LLOYD PITTMAN,
Attorney General
FRANK SPENCER
Assistant Attorney General
W. GLENN WATTS
Special Assistant Attorney General
Post Office Box 220
Jackson Mississippi 39205

CUPIT & MAXEY
304 North Congress Street
Post Office Box 22666
Jackson, Mississippi 39205

APPENDIX

(8)

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI EX REL.
EDWIN LLOYD PITTMAN, ATTORNEY GENERAL
OF MISSISSIPPI, AND
MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

APPENDIX TO MOTION TO DISMISS

Edwin Lloyd Pittman
Attorney General
State of Mississippi

Frank Spencer
Assistant Attorney General
W. Glenn Watts
Special Assistant Attorney General
P.O. Box 220
Jackson Mississippi 39205

*John L. Maxey II
Cupit & Maxey
304 North Congress St.
P.O. Box 22666
Jackson, Mississippi 39205

*Counsel of Record

CASILLAS PRESS INC. — 1717 K STREET NW WASHINGTON DC 20036 — 223-1220

68 pp

TABLE OF CONTENTS

APPENDIX

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSISSIPPI

IN RE:	PETITION OF MISSISSIPPI POWER & LIGHT COMPANY, A MISSISSIPPI CORPORATION, (COMPANY) AND MIDDLE SOUTH ENERGY, INC., AN ARKANSAS CORPORATION, (MSEI) FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO CONSTRUCT, OWN AND OPERATE A TWO UNIT NUCLEAR-FUELED ELECTRIC GENERATING PLANT HAVING AN EXPECTED AGGREGATE CAPACITY OF 2,500 MW, AND NECESSARY RELATED FACILITIES, TO BE LOCATED NORTHWEST OF PORT GIBSON, MISSISSIPPI, IN SECTION 12, TOWNSHIP 12 NORTH, RANGE 2 EAST, CLAIBORNE COUNTY, MISSISSIPPI, KNOWN AS THE GRAND GULF NUCLEAR STATION PROJECT.
MISSISSIPPI POWER & LIGHT COMPANY ELECTRIC BUILDING JACKSON, MISSISSIPPI MIDDLE SOUTH ENERGY, INC. ELECTRIC BUILDING JACKSON, MISSISSIPPI	

JOINT PETITION

Now comes Mississippi Power & Light Company, a corporation organized and existing under and by virtue of the laws of the State of Mississippi ("Company"), and Middle South Energy, Inc., a corporation organized and existing under and by virtue of the laws of Arkansas, but qualified to do business within the State of Mississippi (MSEI), sometimes hereinafter referred to as "Petitioners," and petition this Honorable Commission for a certificate that the present and future public convenience and necessity require, or will require, that Petititoners be given the right to construct, own and operate a two unit nuclear-fueled electric generating plant having an expected aggregate capacity of 2,500 MW, and necessary related facilities, to be located northwest of Port Gibson, Mississippi, in Section 12, Township 12 North, Range 2 East, Claiborne County, Mississippi, known as the Grand Gulf Nuclear Electric

Station Project (Grand Gulf Project); and which certificate will permit Petitioners to construct, own, acquire, extend and operate equipment for the generation, transmission and distribution of electricity for intrastate sales to and for the public for compensation and for grounds of said Petition, would show unto the Commission the following facts, to-wit:

1.

That Company is a utility, as defined in Section 1 D(1) of the Public Utilities Act of 1956, Chapter 372, Mississippi Laws of 1956, as amended, (Sec. 77-3-1, et seq., Mississippi Code of 1972), hereinafter referred to as the "Act."

That MSEI proposes to operate as a generating company owning, financing and operating electric generating facilities for the Middle South Utilities, Inc. System, including the Grand Gulf Project within the State of Mississippi. Therefore, the construction, acquisition, extension and operation of Company's facilities, as well as its service areas and the proposed ownership and operation of the Grand Gulf Project by MSEI, fall under the purview of the aforesaid Act. (Emphasis supplied) That a true and correct copy of Company's Restated Articles of Incorporation, together with all amendments thereto, and together with the Articles of Merger whereunder Company has succeeded to the rights, privileges and properties of Mississippi Power & Light Company, a Florida corporation, are on file with the Commission in Cause U-778, and are incorporated herein by reference. That a true and correct copy of MSEI's Articles of Incorporation, together with its Certificate of Authority to do business in the State of Mississippi, is attached hereto as Exhibit "A" and made a part hereof.

A complete financial statement of Company is likewise on file with this Commission and is incorporated herein by

reference. Having only been organized a short time and not yet undertaken its initial major financing, MSEI's financial statement is not filed herewith; however, MSEI's and Company's ability to finance the construction, ownership and operation of the Grand Gulf Project is hereinafter set out in this Petition.,

That Company is, and together with its predecessor companies, has been for many years engaged in the business of an electric public utility within the western half of Mississippi, inlcuding Claiborne County, where it maintains and has for some time maintained generating stations, transmission lines, transformer stations, distribution lines and other facilities and equipment used and useful in its business as an electric public utility, and particularly in serving its customers and service areas.

That heretofore on the 8th day of August, 1956, Company's predecessor company filed its application with the Commission under Section 5(b) of the said Act, wherein, among other things, its facilities and oprations within Mississippi, including Claiborne County, were set out in detail. That by said Petition and Application, Company, through its predecessor company, has claimed the right to continue to operate its facilities within certain areas of the western one-half of the State of Mississippi, including Claiborne County, as the same existed on the effective date of the said Act, to-wit: March 29, 1956.

That the aforesaid Petition and Application in Cause U-44, together with all exhibits, is incorporated hereby by reference.

That this Commission did by Orders dated December 3, 1958; November 25, 1959; December 12, 1960; May 14, 1962; August 22, 1962; September 5, 1967; January 3, 1968; May 21, 1968; September 3, 1968; and October 1,

1968, in Cause No. U-44, grant unto Company and Company's predecessor, Interim, Partial and Permanent Certificates of Public Convenience and Necessity to operate in various areas and counties of Western Mississippi, including certain areas of Claiborne County, Mississippi, as an electric public utility, pursuant to Section 5(b) of the Act. That Company has now succeeded to the rights so granted to its predecessor, as set forth in Cause U-778 before this Commission. That Company does hereby incorporate by reference all of the aforesaid Orders in Cause U-44. On February 12, 1973, in Docket U-2497, this Commission did grant unto Company a Certificate of Public Convenience and Necessity to acquire the electric distribution system of Capital Electric Power Association and authorized and approved the transfer of all Certificates of Public Convenience and Necessity of Capital Electric Power Association to Company. On March 31, 1973, Company did acquire the system of Capital Electric Power Association, together with all Certificates of Public Convenience and Necessity issued to Capital Electric Power Association by this Commission, said system and Certificates including facilities and service areas in Claiborne County. Company does hereby incorporate the aforesaid Order in Docket U-2497 dated February 12, 1973, in this Petition by reference.

2.

Middle South Utilities, Inc. ("Middle South") is a holding company registered under the Public Utility Holding Company Act of 1935. It owns all of the outstanding common stock of each of its principal operating subsidiaries: Arkansas Power & Light Company (Arkansas), Arkansas-Missouri Power Company (Ark-Mo), Louisiana Power & Light Company (Louisiana), Company, and New

Orleans Public Service Inc. (NOPSI) (collectively, System operating companies and, singly, System operating company). Middle South also owns all of the outstanding common stock of Crossett Electric Company, the properties of which are leased to Arkansas, and all of the outstanding common stock of Middle South Services, Inc. (Services), a subsidiary service company. Middle South and all of its subsidiaries constitute the Middle South Utilities System (Middle South System). The electric properties of the System operating companies constitute an integrated public utility system.

The electric power generating facilities of the Middle South System are primarily steam electric facilities strategically located with reference to the availability of fuel, protection of local loads and other controlling economic factors. These facilities are interconnected by a transmission system operating at voltages of 115KV and higher. In each instance, facilities are owned by the System operating company serving the area in which the facilities are located.

Historically, the financing of such facilities has been carried out by the System operating companies primarily through the sales of their first mortgage bonds and preferred stock to the public. Middle South has provided the common equity portion of the permanent capital needs of the System operating companies through the purchase of common stock of these companies.

The anticipated power needs of existing customers and the additional load imposed by expected new customers have required the System operating companies to plan the installation of massive amounts of new generating capacity. These power needs have required the construction of increasingly larger and more expensive generating units by the System operating companies.

The following table shows this trend with respect to the major generating units which have been and are to be added to the Middle South System between 1974 and 1976 (99% of all planned additions to the Middle South System for the period). Financing for these units has either been completed or definitively planned by the System operating companies involved.

Company	Unit	MW	Cost (Millions)	Per KW	On-Line Date
Louisiana	Waterford No. 1	430	$ 55	$129	1974
Arkansas	Arkansas Nuclear One Unit No. 1*	850	$211	$249	1974
Louisiana	Waterford No. 2	430	$ 55	$129	1975
Company	Andrus No. 1	750	$107	$143	1975
Arkansas	Arkansas Nuclear One Unit No. 2*	950	$275	$289	1976

*Excludes fuel core costs.

It should be noted that the cost per KW of installed capacity has risen dramatically due to the ever-increasing costs of materials and labor. The units shown above thus have a projected average capacity of 682,000 KW and a projected average cost of $141 million, or $206 per KW. For purposes of comparison, at December 31, 1973, the average Middle South System major generating unit had a capacity of 212,000 KW and its original cost was $18.1 million, or $85 per KW.

In addition, factors beyond the control of the System operating companies have substantially increased the time

necessary to construct and start up new units over the time formerly experienced. Fossil fuel plants which used to be built in 30 to 36 months, now take 48 months to complete. Nuclear plants take at least 7 to 8 years, and in some cases, depending upon licensing and other delays, even longer. Contracts for the engineering and construction of these units include provisions for escalation related to certain construction costs indices. Thus, the longer construction times, coupled with expected inflationary pressures, can only increase the cost.

Pursuant to the Middle South Systems planning procedures, Company has been undertaking the engineering and necessary related work in connection with the Grand Gulf Project, a two-unit nuclear plant to be constructed in its operating area. These units have a projected 1,250 MW capability each and an estimated aggregate cost of $1,227 million, with on-line dates of 1979 and 1981.

For purposes of comparison the following should be noted: at December 31, 1973, the Middle South System's total installed generating capability of 9,141 MW cost $787 million when new. Yet the cost of the first Grand Gulf unit will equal 84% of this total. And at the end of 1973, Company's total capitalization was $393 million, compared with the estimated aggregate cost of the Grand Gulf Project of $1,227 million; the first Grand Gulf unit alone will cost 148% of Company's year-end plant account.

The generating facilities of the Middle South System have been strategically located with a reference to the availability of fuel, protection of local loads and other controlling economic factors. The size of these units has been determined basically by the projected load growth of the Middle South System. Company's present rate and

capital structure obviously cannot support construction of this magnitude.

In order to finance this construction on a basis that will be in the best interests of both its investors and the investors in its subsidiaries, and to insure adequate and dependable electric service to the customers and service areas of its subsidaries, including Company, and without unnecessarily complicating its financial structure, Middle South has organized Middle South Energy, Inc. (MSEI).

3.

MSEI is a corporation organized under the laws of the State of Arkansas and qualified to do business in Mississippi. It proposes to function as a generating company owning and financing generating facilities for the Middle South System including facilities within Mississippi. As a first step in this plan, MSEI proposes to acquire the Grand Gulf Project, which as noted above, will consist of two nuclear-powered units of 1250 MW each scheduled to be operational by September, 1979 and September, 1981, respectively, reimbursing Company for its expenditures to date in connection therewith. MSEI will thus assume the ownership of the Grand Gulf Project and be primarily responsible for its financing, construction and operation. Company has commenced the engineering for the project and has applied to the United States Atomic Energy Commission (AEC) for a construction permit for each unit. MSEI proposes to become a co-applicant with Company for the necessary AEC construction permits and operating licenses.

Petitioners propose that under contract with MSEI the design, construction, maintenance and operation of the Grand Gulf Project will be performed by Company. These functions will be carried out for MSEI by Company pur-

suant to a service agreement ("Service Agreement") with MSEI.

Pursuant to a Sales Agreement, MSEI will acquire from Company, and Company will transfer and assign to MSEI, (i) all of the property owned by Company and constituting the Grand Gulf Project, consisting chiefly of land, engineering and design work and licensing costs and (ii) all of Company's right, title and interest in and to any contracts, agreements and purchase orders in connection with equipment or other facilities and materials and supplies, purchased or contracted to be purchased by Company for the Grand Gulf Project, in exchange for cash equal to the original cost of such property, which at December 31, 1973, amounted to approximately $19,600,000 million.

4.

Pursuant to an agreement among Arkansas, Ark-Mo., Louisiana, Company, NOPSI and Services dated April 16, 1973 (System Agreement), as amended, the System operating companies which have built generating capacity in excess of their current area requirements sell such power as they do not utilize to the other System operating companies. In return the purchasers agree to take such power and pay therefor sufficient monies to provide for the normal operating expenses, fixed charges on debt and a fair rate of return on the investment in such facility of the selling company. The System Agreement has been accepted for filing with the Federal Power Commission in Docket No. E-8130 and that Commission, by order of February 7, 1974, provided for the revision of certain service schedules thereto.

In the event that the Grand Gulf Project were permanently shut down, and in certain other circumstances, MSEI would receive no payments under the System Agree-

ment. Therefore, it is proposed that a supplement to the System Agreement (Availability Agreement) be executed whereby MSEI would receive certain commitments from the other parties thereto with respect to the payment of certaining operating, maintenance and shut-down costs.

Under the Availability Agreement, MSEI will agree with the System operating companies to undertake to use its best efforts to construct the Grand Gulf Project and to make all power generated thereby available to the System operating companies pursuant to the System Agreement.

5.

Thus Petitioners pursuant to various agreements heretofore referred to will jointly be engaged in the construction, ownership and operation of electric facilities for the generation of electricity for sales to or for the public for compensation within Mississippi and, therefore, seek a Certificate of Public Convenience and Necessity therefor as set out and described in this Joint Petition. The Grand Gulf Project will generate electricity which will be used by Company to render service to all those customers and service areas which it is legally entitled to serve.

6.

Petitioners propose to construct, own and operate the Grand Gulf Project which will consist of a two unit nuclear-fueled electric generating plant having an expected aggregate capacity of 2500 MW, and necessary related facilities. Each of the twin boiling water reactors will supply steam to a turbine generator with a capacity of 1,313 MW gross and 1250 MW net, with associated transformer, switch yard, supporting buildings and additional auxiliary systems and facilities as required.

The Grand Gulf Project will be located on a site in Section 12, Township 12 North, Range 2 East, Claiborne County, Mississippi. This site is on the east bank of the Mississippi River approximately 25 miles south of Vicksburg, Mississippi, 37 miles north of Natchez, Mississippi, and approximately five miles northwest of Port Gibson, Mississippi. The site for the entire Grand Gulf Station Project consists of approximately 2,300 acres, although the nuclear electric plant will be located on approximately 300 acres within the aforesaid 2300 acres. There is attached hererto marked Exhibit "B" and made a part hereof, a map of Claiborne County on a scale of 1/2 inch to the mile showing thereon by a blue shaded area the proposed site of the Grand Gulf Project with the generating plant being shown within said site by a red square.

7.

Petitioners propose that site preparation work on both units will start immediately, making it possible for Petitioners to meet the currently scheduled operational dates of September, 1979 for Unit 1 and September, 1981 for Unit 2. Petitioners would show unto the Commission that construction work should begin as soon as possible to insure completion of Unit 1 in time to meet the 1980 load schedule. Any delay in the start of construction or any delay in meeting the currently scheduled operational dates will mean the Middle South System power reserve will drop to a seriously low level in 1980 and total construction costs for the plant will increase substantially.

Fuel for the Grand Gulf Project reactors consists of cemanic pellets of slightly enriched uranium dioxide encapsulated in zirconium rods. Present plans call for the gradual insertion in later fuel cycles of plutonium oxide

pellets. This plutonium, also a valuable nuclear fuel, will have been generated as a by-product of earlier reactor operation.

The entire 2300 acres composing the proposed site of the Grand Gulf Project are located within the Grandfather Service Area of Southwest Mississippi Electric Power Association, Lorman, Mississippi.

Company proposes to construct a 115 KV transmission line from Company's Port Gibson 115 KV Substation to the proposed generating plant site for construction power and additional trasnmission and distribution facilities as may be needed to tie the aforesaid generating plant into Company's System within Mississippi and the electric systems of the other operating companies of the Middle South System. Company will seek authority for construction of the aforesaid transmission and distribution facilities under separate petitions or applications to this Commission.

8.

There is attached hereto marked Exhibit "C" and made a part hereof a map of the Middle South Utilities System's generation and transmission facilities. Also shown on said map is the proposed site of the Grand Gulf Project. There is also attached hereto as Exhibit "D" a system map of Company showing thereon the proposed site of the Grand Gulf Project.

9.

Petitioners would show unto the Commission that Company has heretofore made application to the United States Atomic Energy Commission for the necessary construction permit pursuant to the provisions of the Atomic

Energy Commission's Rulès and Regulations. The aforesaid Application, as Amended, contains all general information required concerning the Grand Gulf Project, the technical information and safety analysis report concerning both units of said Nuclear Station, and Environmental Report and such other documents as required for the granting of said Application. MSEI proposes to become a joint applicant with Company in the aforesaid Application now pending before the United States Atomic Energy Commission in Docket Nos. 50-416 and 50-417. Petitioners anticipate receiving all necessary approvals from the Atomic Energy Commission in due course thereby enabling Petitioners to begin site preparation work and other construction as heretofore set out. Further, Petitioners would show unto this Commission that the Grand Gulf Project will, in all respects, meet the safety and environmental standards necessary for its construction, ownership and operation.

10.

The proposed two 1250 MW generating units for the Grand Gulf Project will serve as a major source of base-load capacity for the Company and the entire Middle South System pooling arrangement. The proposed two units are necessary in order to provide capability with adequate reserves to Company and to the Middle South System to serve the projected electric loads of Western Mississippi and the entire area served by the Middle South System. Electric loads of Company and of the Middle South System have grown rapidly over the past years and are projected to continue this growth in the future. On the basis of load projections for the next ten years, it will be necessary for the Middle South System, of which Company is a part, to add major units of generating capacity

each year to maintain the capability required to carry the loads with adequate reserves. There is attached hereto marked Exhibit "E" and "F," respectively, and made a part hereof the same as if copied herein in words and figures, a table showing thereon Company's and Middle South System's load and capability forecasts for the 10-year period 1973 through 1983. As shown on said Exhibits "E" and "F," Units 1 and 2 of the Grand Gulf Project are necessary to prevent reserve capacities of Company and the Middle South System from dropping to dangerously low levels. The minimum reserve margin for the Middle South System has been established at 16% based on operating experience over a long period of time. This reserve margin is at the low end of the range considered adequate for most systems in the United States, which, according to the Federal Power Commission, is between 15% and 25% of peak load. Thus, Unit No. 1 is necessary to meet the peak load season fo 1980 in order to preserve the minimum reserve level of 16%.

By virtue of the fact that Company is a part of the Middle South System which is an integrated electric system, Company will have available for its customers such capability of the entire Middle South System as may be necessary for carrying Company's loads during the period of time reflected by the above schedules.

In order that Company may render adequate and dependable service to its customers and service areas pursuant to authority granted to Company by this Commission, it is necessary that Petitioners construct, own and operate the two units of the Grand Gulf Nuclear Station Project as proposed herein.

11.

The proposed site of the Grand Gulf Project is a most favorable location electrically to supply the loads of Company's system and is centrally located in relation to the Middle South System. The location is favorable for connection of the generating plant to the existing transmission facilities of Company and the Middle South System. The river location is advantageous to the operation of said project. The location of the Grand Gulf Project affords maximum advantages consistent with safety and environmental factors concerning a nuclear station.

12.

As stated earlier, Units No. 1 and 2 of the Grand Gulf Project are estimated to cost in total approximately $1,227,000,000. It has been determined that it is economically and financially feasible to concentrate the financing and ownership of Middle South System's future base load generation in MSEI. Middle South Utilities, Inc. and MSEI will enter into a capital fund agreement, pursuant to which Middle South will agree to supply or cause to be supplied such amounts of capital, in addition to (i) the capital made available to MSEI by Middle South as the purchase price of the Grand Gulf Project, and (ii) the amount to be made available under a bank loan agreement, as shall be required in order to complete the construction of the Grand Gulf Projects, to permit the commercial operation of the steam electric generating units and to permit continued commercial operation over the expected life of the units. Subject to Securities and Exchange Commission approval, the money required for the construction, ownership and operation of the Grand Gulf Project will be supplied in part from cash generated through operation and in part from the sale from time to

time of notes, debentures bonds, preferred stock, common stock or any or all of them as required and as may be deemed appropriate in the light of MSEI's, Company's and Middle South's position and the market conditions prevailing at the time.

13.

That Petitioners desire a Certificate of Public Convenience and Necessity from this Commission to permit Petitioners to construct, own and operate the aforesaid two units of the Grand Gulf Nuclear Electric Station Project, together with all component parts thereof, and related facilities necessary and required for the operation of same.

Petitioners would show unto the Commission that the public convenience and necessity require that the two units of the Grand Gulf Project be constructed, owned and operated by Petitioners in the manner and form as set out here in order for Company to meet the projected loads on Company's system and render adequate and dependable electric service to the customers and service areas of Company.

14.

That although the general site of the genrating plant is shown on exhibits hereto, the actual location of said generating plant on the site will depend on ground surveys and terrain accessibility and nature of the area. Petitioners request that the construction of the aforesaid generating units be approved, together with any additional land acquisitions that may be necessary, with the exact site of the generating units to be determined as above stated.

That the only other persons who may be affected by the subject matter of this Petition are:

Central Electric Power Association
Carthage, Mississippi

Delta Electric Power Association
Greenwood, Mississippi

East Mississippi Electric Power Association
Meridian, Mississippi

Four County Electric Power Association
Columbus, Mississippi

Magnolia Electric Power Association
McComb, Mississippi

Natchez Trace Electric Power Association
Houston, Mississippi

North Central Mississippi Electric Power Association
Coldwater, Mississippi

Pearl River Valley Electric Power Association
Columbia, Mississippi

South Mississippi Electric Power Association
Hattiesburg, Mississippi

Southern Pine Electric Power Association
Tyalorsville, Mississippi

Southwest Mississippi Electric Power Association
Lorman, Mississippi

Tallahatchie Valley Electric Power Association
Batesville, Mississippi

Twin County Electric Power Association
Hollandale, Mississippi

West Mississippi Electric Power Association
Greenwood, Mississippi

Yazoo Valley Electric Power Association
Yazoo City, Mississippi

Mississippi Power Company
Gulfport, Mississippi

Board of Supervisors
Claiborne County
Port Gibson, Mississippi

Canton Municipal Utilities
City of Canton
Canton, Mississippi

Kosciusko Water & Light Plant
City of Kosciusko
Kosciusko, Mississippi

Leland Water & Light Plant
City of Leland
Leland, Mississippi

Durant Water & Light Plant
City of Durant
Durant, Mississippi

Clarksdale Water & Light Department
City of Clarksdale
Clarksdale, Mississippi

Greenwood Utilities
City of Greenwood
Greenwood, Mississippi

Yazoo City Public Service Commission
City of Yazoo City
Yazoo City, Mississippi

City of Port Gibson
Port Gibson, Mississippi

15.

Petitioners are ready, willing and able to construct, own and operate Units 1 and 2 of the Grand Gulf Project, all components necessary thereto and all related facilities, as applied for herein, and to operate the same and to render adequate electric service to all persons and premises which they may be legally entitled to serve. The present and future public convenience and necessity require and will require that Petitioners be granted by this Commission a Certificate of Public Convenience and Necessity to acquire, extend, construct, own and operate the facilities as herein described and applied for.

WHEREFORE, PREMISES CONSIDERED, Petitioners pray that this Honorable Commission will set this matter for hearing at an early date, and particularly pray that this Commission shall find that the public convenience and necessity require that such hearing be held at the earliest date available, and Petitioners further pray that process be issued by this Commission in the manner provided by law and the Rules and Regulations of this Commission, giving reasonable notice of the hearing hereof to all interested persons, as in its judgment may be necessary, including the time and place of such hearing and the purpose thereof, and Petitioners particularly pray that such notice be given to those utilities, municipalities and persons listed in Paragraph 14 of this Petition which are the utilities and persons that may be affected by the subject matter of this Petition.

Petitioners further pray that upon the hearing prayed for, this Commission shall grant a Certificate that the Public Convenience and Necessity require, and will require, that Petitioners acquire the necessary property, easements, and rights of way and extend, acquire, construct, own and operate Units No. 1 and 2 of the Grand Gulf Project, together with all components necessary thereto and all related facilities, all as herein particularly described and hereby applied for and to operate the same for the generation, transmission and distribution of electricity for intrastate sales to and for the public for compensation, as the same are fully described and applied for in this Petition.

Respectfully submitted,

MISSISSIPPI POWER & LIGHT COMPANY

and

MIDDLE SOUTH ENERGY, INC.

BY: WISE CARTER CHILD STEEN & CARAWAY
THEIR ATTORNEYS

BY: /s/ James K. Child

FILED
APRIL 12 1974
MISS. PUBLIC SERVICE
COMMISSION

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSISSIPPI

MISSISSIPPI POWER & LIGHT COMPANY
ELECTRIC BUILDING
JACKSON, MISSISSIPPI

MIDDLE SOUTH ENERGY, INC.
ELECTRIC BUILDING
JACKSON, MISSISSIPPI

IN RE: PETITION OF MISSISSIPPI POWER & LIGHT COMPANY, A MISSISSIPPI CORPORATION, (COMPANY) AND MIDDLE SOUTH ENERGY, INC., AN ARKANSAS CORPORATION, (MSEI) FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO CONSTRUCT, OWN AND OPERATE A TWO UNIT NUCLEAR-FUELED ELECTRIC GENERATING PLANT HAVING AN EXPECTED AGGREGATE CAPACITY OF 2,500 MW, AND NECESSARY RELATED FACILITIES, TO BE LOCATED NORTHWEST OF PORT GIBSON, MISSISSIPPI, IN SECTION 12, TOWNSHIP 12 NORTH, RANGE 2 EAST, CLAIBORNE COUNTY, MISSISSIPPI, KNOWN AS THE GRAND GULF NUCLEAR STATION PROJECT.

ORDER GRANTING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

This cause came on to be heard and was heard on the 23rd day of May, 1974, at 10:00 A.M. in the offices of the Mississippi Public Service Commission on the Nineteenth Floor of the Sillers State Office Building, Jackson, Mississippi, on the Joint Petition of Mississippi Power & Light Company, a corporation organized and existing under and by virtue of the laws of the State of Mississippi ("Company"), and Middle South Energy, Inc., a corporation organized and existing under and by virtue of the laws of Arkansas, but qualified to do business within the State of Mississippi (MSEI), sometimes hereinafter referred to as "Petitioners," for a certificate that the present and future public convenience and necessity require, or will require, that Petitioners be given the right to construct, own and operate a two unit nuclear-fueled electric generating plant having an expected aggregate capacity of 2,500 MW, and necessary related facilities, to be located northwest of

Port Gibson, Mississippi, in Section 12, Township 12 North, Range 2 East, Claiborne County, known as the Grand Gulf Nuclear Electric Station Project ("Grand Gulf Project"); and which certificate will permit Petitioners to construct, own, acquire, extend and operate equipment for the generation, transmission and distribution of electricity for intrastate sales to and for the public for compensation; and

Petitioners introduced evidence, both oral and documentary, in support of their Joint Petition, and the Commission having heard and considered the matter and being fully advised in the premises, finds as follows, to-wit:

That said Joint Petition was filed with the Commission on April 12, 1974, by Petitioners, and that subsequent thereto by Order of the 15th day of April, 1974, the Commission set the above matter for hearing on May 7, 1974, and notice of said hearing was given to all persons interested therein by publication in a newspaper of general circulation published in Jackson, Mississippi, to-wit: "The Clarion Ledger" on April 16, 1974, and by mailing such notice by registered or certified mail on the 15th day of April, 1974, to each public utility or persons interested therein and which may be affected by an order resulting from said Petition and hearing, and particularly to:

Central Electric Power Association
Carthage, Mississippi

Delta Electric Power Association
Greenwood, Mississippi

East Mississippi Electric Power Association
Meridian, Mississippi

Four County Electric Power Association
Columbus, Mississippi

Magnolia Electric Power Association
McComb, Mississippi

Natchez Trace Electric Power Association
Houston, Mississippi

North Central Mississippi Electric Power Association
Coldwater, Mississippi

Pearl River Valley Electric Power Association
Columbia, Mississippi

South Mississippi Electric Power Association
Hattiesburg, Mississippi

Southern Pine Electric Power Association
Tyalorsville, Mississippi

Southwest Mississippi Electric Power Association
Lorman, Mississippi

Tallahatchie Valley Electric Power Association
Batesville, Mississippi

Twin County Electric Power Association
Hollandale, Mississippi

West Mississippi Electric Power Association
Greenwood, Mississippi

Yazoo Valley Electric Power Association
Yazoo City, Mississippi

Mississippi Power Company
Gulfport, Mississippi

Board of Supervisors
Claiborne County
Port Gibson, Mississippi

Canton Municipal Utilities
City of Canton
Canton, Mississippi

Kosciusko Water & Light Plant
City of Kosciusko
Kosciusko, Mississippi

Leland Water & Light Plant
City of Leland
Leland, Mississippi

Durant Water & Light Plant

City of Durant
Durant, Mississippi

Clarksdale Water & Light Department
City of Clarksdale
Clarksdale, Mississippi

Greenwood Utilities
City of Greenwood
Greenwood, Mississippi

Yazoo City Public Service Commission
City of Yazoo City
Yazoo City, Mississippi

City of Port Gibson
Port Gibson, Mississippi

The Commission did by order dated May 7, 1974, continue this cause from May 7, 1974, the date originally set for hearing, at which time no persons appeared and no objections had been filed, and set this cause for special hearing at 10:00 A.M. Thursday, May 23, 1974, and notice of said continuance, order and hearing was mailed to each person and public utility interested therein, including those persons specifically set out above, as is required by law and having been given in strict compliance with law, and said notices being in the judgment of the Commission such reasonable notice of said hearing to all interested persons as is necessary under the law and under the rules and regulations of this Commission; and

That said notices were so published and so mailed, and set forth sufficient identification of the cause, place, date and hour of said hearing as aforesaid, and a brief statement of the nature of the matter involved; that proof of publication of the notice was filed in this cause before the hearing, and notation was made on the docket herein of the names of the persons to whom the notice was mailed; and

That the Commission has jurisdiction of the parties and of the subject matter, and jurisdiction to do that hereunder done in manner and form as done; and

That no objections or protests to the granting of a Certificate to the Petitioners herein have been filed, and that no protestants appear and no objections are made to the granting of this order; and

That Company is a utility, as defined in Section 1 D(1) of the Public Utilities Act of 1956, Chapter 372, *Mississippi Laws of 1956,* as amended, (Sec. 77-3-1, et seq., *Mississippi Code of 1972),* hereinafter referred to as the "Act."

That MSEI proposes to operate as a generating company owning, financing and operating electric generating facilities for the Middle South Utilities, Inc., System, includig the Grand Gulf Project within the State of Mississippi. Therefore, the construction, acquisition, extension and operation of Company's facilities, as well as its service areas and the proposed ownership and operation of the Grand Gulf Project by MSEI, fall under the purview of the aforesaid Act. That a true and correct copy of Company's Restated Articles of Incorporation, together with all amendments thereto that date, and together with the Articles of Merger whereunder Company has succeeded to the rights, privileges and properties of Mississippi Power & Light Company, a Florida corporation, are on file with the Commission in Cause U-778, and are incorporated in the Joint Petition and record of this cause by reference. That a true and correct copy of MSEI's Articles of Incorporation, together with its Certificate of Authority to do business in the State of Mississippi, is attached to the Joint Petition as Exhibit "A" and made a part thereof. That Company's Restated Articles of Incorporation are filed

with this Commission in Docket U-2751 and incorporated in the record of this cause by reference.

A complete financial statement of Company is likewise on file with this Commission and is incorporated in the Joint Petition by reference and Company's Annual Report for 1973 is in the record of this cause. Having only been organized a short time and not yet undertaken its initial major financing MSEI's financial statement is not filed in this cause; however, MSEI's and Company's ability to finance the construction, ownership and operation of the Grand Gulf Project is fully set out in the Joint Petition and record of this cause.

That Company is, and together with its predecessor companies, has been for many years engaged in the business of an electric public utility within the western half of Mississippi, including Claiborne County, where it maintains and has for some time maintained generating stations, transmission lines, transformer stations, distribution lines and other facilities and equipment used and useful in its business as an electric public utility, and particularly in serving its customers and service areas.

That heretofore on the 8th day of August, 1956, Company's predecessor company filed its application with the Commission under Section 5(b) of the said Act, wherein, among other things, its facilities and operations within Mississippi, including Claiborne County, were set out in detail. That by said Petition and Application, Company, through its predecessor company, has claimed the right to continue to operate its facilities within certain areas of the western one-half of the State of Mississippi, including Claiborne County, as the same existed on the effective date of the said Act, to-wit: March 29, 1956.

That the aforesaid Petition and Application in Cause U-44, together with all exhibits, is incorporated in the Joint Petition herein and record of this cause by reference. That this Commission did by Orders dated December 3, 1985; November 25, 1959; December 12, 1960; May 14, 1962; August 22, 1962; September 5, 1967; January 3, 1968; May 21, 1968; September 3, 1968; and October 1, 1968, in Cause No. U-44, grant unto Company and Company's predecessor Interim, Partial and Permanent Certificates of Public Convenience and Necessity to operate in various areas and counties of Western Mississippi, including certain areas of Claiborne County, Mississippi, as an electric public utility, pursuant to Section 5(b) of the Act. That Company has now succeeded to the rights so granted to its predecessor, as set forth in Cause U-778 before this Commission. That Company did incorporate by reference all of the aforesaid Orders in Cause U-44 in the Joint Petition and record of this cause.

On February 12, 1973, in Docket U-2497, this Commission did grant unto Company a Certificate of Public Convenience and Necessity to acquire the electric distribution system of Capital Electric Power Association and authorized and approved the transfer of all Certificates of Public Convenience and Necessity of Capital Electric Power Association to Company. On March 31, 1973, Company did acquire the system of Capital Electric Power Association, together with all Certificates of Public Convenience and Necessity issued to Capital Electric Power Association by this Commission, said system and Certificates including facilities and service areas in Claiborne County. Company did incorporate the aforesaid Order in Docket U-2497 dated February 12, 1973 in the Joint Petition by reference.

Middle South Utilizies, Inc. ("Middle South") is a holding company registered under the Public Utility Hold-

ing Company Act of 1935. It owns all of the outstanding common stock of each of its principal operating subsidiaries: Arkansas Power & Light Company (Arkansas), Arkansas-Missouri Power Company (Ark-Mo), Louisiana Power & Light Company (Louisiana), Company, and New Orleans Public Service Inc. (NOPSI) (collectively, System operating companies and, singly, System operating company). Middle South also owns all of the outstanding common stock of Crossett Electric Company, the properties of which are leased to Arkansas, and all of the outstanding common stock of Middle South Services, Inc. (Services), a subsidiary service company. Middle South and all of its subsidiaries constitute the Middle South Utilities System (Middle South System). The electric properties of the System operating companies constitute an integrated public utility system.

The electric power generating facilities of the Middle South System are primarily steam electric facilities strategically located with reference to the availability of fuel, protection of local loads and other controlling economic factors. These facilities are interconnected by a transmission system operating at voltages of 115 KV and higher. In each instance, facilities are owned by the System operating company serving the area in which the facilities are located.

Historically, the financing of such facilities has been carried out by the System operating companies primarily through the sales of their first mortgage bonds and preferred stock to the public. Middle South has provided the common equity portion of the permanent capital needs of the System operating companies through the purchase of common stock of these companies.

The anticipated power needs of existing customers and the additional load imposed by expected new customers

have required the System operating companies to plan the installation of massive amounts of new generating capacity. These power needs have required the construction of increasingly larger and more expensive generating units by the System operating companies.

The following table shows this trend with respect to the major generating units which have been and are to be added to the Middle South System between 1974 and 1976 (99% of all planned additions to the Middle South System for the period). Financing for these units has either been completed or definitely planned by the System operating companies involved.

Company	Unit	MW	Cost (Millions)	Per KW	On-Line Date
Louisiana	Waterford No. 1	430	$ 55	$129	1974
Arkansas	Arkansas Nuclear One Unit No. 1*	850	$211	$249	1974
Louisiana	Waterford No. 2	430	$ 55	$129	1975
Company	Andrus No. 1	750	$107	$143	1975
Arkansas	Arkansas Nuclear One Unit No. 2*	950	$275	$289	1976

*Excludes fuel core costs.

It should be noted that the cost per KW of installed capacity has risen dramatically due to the ever-increasing costs of materials and labor. The units shown above thus have a projected average capacity of 682,000 KW and a projected average cost of $141 million, or $206 per KW. For purposes of comparison, at December 31, 1973, the average Middle South System major generating unit had a

capacity of 212,000 KW and its original cost was $18.1 million, or $85 per KW.

In addition, factors beyond the control of the System operating companies have substantially increased the time necessary to construct and start up new units over the time formerly experienced. Fossil fuel plants which used to be built in 30 to 36 months, now take 48 months to complete. Nuclear plants take at least 7 to 8 years, and in some cases, depending upon licensing and other delays, even longer. Contracts for the engineering and construction of these units include provisions for escalation related to certain construction costs indices. Thus, the longer construction times, coupled with expected inflationary pressures, can only increase the cost.

Pursuant to the Middle South Systems planning procedures, Company has been undertaking the engineering and necessary related work in connection with the Grand Gulf Project, a two-unit nuclear plant to be constructed in its operating area. These units have a projected 1,250 MW capability each and an estimated aggregate cost of $1,227 million, with completion dates scheduled for the peak loads of 1980 and 1982.

For purposes of comparison the following should be noted: at December 31, 1973, the Middle South System's total installed generating capability of 9,141 MW cost $787 million when new. Yet the cost of the first Grand Gulf unit will equal 84% of this total. And at the end of 1973, Company's total capitalization was $393 million, compared with the estimated aggregate cost of the Grand Gulf Project of $1,227 million; the first Grand Gulf unit alone will cost 148% of Company's year-end plant account.

The generating facilities of the Middle South System have been strategically located with a reference to the

availability of fuel, protection of local loads and other controlling economic factors. The size of these units has been determined basically by the projected load growth of the Middle South System. Company's present rate and capital structure obviously cannot support construction of this magnitude.

In order to finance this construction on a basis that will be in the best interests of both its investors and the investors in its subsidiaries, and to insure adequate and dependable electric service to the customers and service areas of its subsidaries, including Company, and without unnecessarily complicating its financial structure, Middle South has been organized.

MSEI is a corporation organized under the laws of the State of Arkansas and qualified to do business in Mississippi. Subject to receipt of appropriate approvals from the Securities and Exchange Commission, it proposes to function as a generating company owning and financing generating facilities for the Middle South System including facilities within Mississippi. As a first step in this plan, MSEI proposes to acquire the Grand Gulf Project, reimbursing Company for its expenditures to date in connection therewith. MSEI will thus assume the ownership of the Grand Gulf Project and be primarily responsible for its financing, construction and operation. Company has commenced the engineering for the project and has applied to the United States Atomic Energy Commission (AEC) for a construction permit and all necessary licenses for each unit. MSEI proposes to become a co-applicant with Company for the necessary AEC construction permits and operating licenses.

Petitioners propose that under contract with MSEI the design, construction, maintenance and operation of the

Grand Gulf Project will be performed by Company. These functions will be carried out for MSEI by Company pursuant to a service agreement ("Service Agreement") with MSEI.

Pursuant to a Sales Agreement, MSEI will acquire from Comany, and Company will transfer and assign to MSEI, (i) all of the property owned by Company and constituting the Grand Gulf Project, consisting chiefly of land, engineering and design work and licensing costs and (ii) all of Company's right, title and interest in and to any contracts, agreements and purchase orders in connection with equipment or other facilities and materials and supplies, purchased or contracted to be purchased by Company for the Grand Gulf Project, in exchange for cash equal to the original cost of such property, which at December 31, 1973, amounted to approximately $19,600,000 million. Copies of the form of the proposed Sales Agreement and Service Agreement are in evidence in the record of the hearing in this cause.

Pursuant to an agreement among Arkansas, Ark-Mo., Louisiana, Company, NOPSI and Services dated April 16, 1973 (System Agreement), as amended, the System operating companies which have built generating capacity in excess of their current area requirements sell such power as they do not utilize to the other System operating companies. In return the purchasers agree to take such power and pay therefor sufficient monies to provide for the normal operating expenses, fixed charges on debt and a fair rate of return on the investment in such facility of the selling company. The System Agreement has been accepted for filing with the Federal Power Commission in Docket No. E-8130 and that Commission, by order of January 7, 1974, provided for the revision of certain service schedules thereto.

It is proposed that an Availability Agreement be executed whereby MSEI would agree with the System operating companies to undertake its best efforts to construct the Grand Gulf Project and to make all power generated thereby available under the terms of the System Agreement. At an appropriate time, the System Agreement will be amended to make MSEI a party thereo.

In the event that the Grand Gulf Project were permanently shut down, and in certain other circumstances, MSEI would receive no payments under the Availability Agreement in amounts sufficient to meet certain operating, maintenance and shut-down costs.

Thus Petitioners pursuant to various agreements heretofore referred to will jointly be engaged in the construction, ownership and operation of electric facilities for the generation of electricity for sales to or for the public for compensation within Mississippi and, therefore, seek a Certificate of Public Convenience and Necessity therefor as set out and described in this Joint Petition. The Grand Gulf Project will generate electricity which will be used by Company to render service to all those customers and service areas which it is legally entitled to serve.

Petitioners propose to construct, own and operate the Grand Gulf Project which will consist of a two unit nuclear-fueled electric generating plant having an expected aggregate capacity of 2500 MW, and necessary related facilities. Each of the twin boiling water reactors will supply steam to a turbine generator with a capacity of 1,313 MW gross and 1,250 MW net, with associated transformer, switch yard, supporting buildings and additional auxiliary systems and facilities as required.

The Grand Gulf Project will be located on a site in Section 12, Township 12 North, Range 2 East, Claiborne

County, Mississippi. This site is on the east bank of the Mississippi River approximately 25 miles south of Vicksburg, Mississippi, 37 miles north of Natchez, Mississippi, and approximately five miles northwest of Port Gibson, Mississippi. The site for the entire Grand Gulf Station Project consists of approximately 2,300 acres, although the nuclear electric plant will be located on approximately 300 acres within the aforesaid 2300 acres. There is attached to the Joint Petition marked Exhibit "B" and made a part hereof, a map of Claiborne County on a scale of 1/2 inch to the mile showing thereon by a blue shaded area the proposed site of the Grand Gulf Project with the generating plant being shown within said site by a red square.

Petitioners propose that site preparation work on both units will start immediately, making it possible for Petitioners to meet the currently scheduled operational dates of September, 1979 for Unit 1 and September, 1981 for Unit 2. That construction should begin as soon as possible to insure completion of Unit 1 in time to meet the 1980 load schedule. Any delay in the start of construction or any delay in meeting the currently scheduled operational dates will mean the Middle South System's ability to meet anticipated load in 1980 will be seriously affected and total construction costs for the plant will increase substantially.

Fuel for the Grand Gulf Project reactors consists of ceramic pellets of slightly enriched uranium dioxide encapsulated in zirconium rods. Present plans call for the gradual insertion in later fuel cycles of plutonium oxide pellets. This plutonium, also a valuable nuclear fuel, will have been generated as a by-product of earlier reactor operation.

The entire 2300 acres composing the proposed site of the Grand Gulf Project are located within the Grandfather

Service Area of Southwest Mississippi Electric Power Association, Lorman, Mississippi.

Company proposes to construct a 115 KV Substation at the plant site and a 115 KV transmission line from Company's Port Gibson 115 KV Substation to the proposed generating plant site for construction power and additional transmission and distribution facilities as may be needed to tie the aforesaid generating plant into Company's System within Mississippi and the electric systems of the other operating companies of the Middle South System. Company will seek authority for construction of the aforesaid transmission and distribution facilities under separate petitions or applications to this Commission.

There is attached to the Joint Petition marked Exhibit "C" and made a part thereof a map of the Middle South Utilities System's generation and transmission facilities. Also shown on said map is the proposed site of the Grand Gulf Project. There is also attached to the Joint Petition as Exhibit "D" a system map of Company showing thereon the proposed site of the Grand Gulf Project as well as Company's generation, transmission and distribution systems.

That Company has heretofore made application to the United States Atomic Energy Commission for the necessary construction permit and all necessary licenses pursuant to the provisions of the Atomic Energy Commission's Rules and Regulations. The aforesaid Application, as Amended, contains all general information required concerning the Grand Gulf Project, technical information, safety analyses, environmental data and such other documents as required for the granting of said Application. MSEI proposes to become a joint applicant with Company in the aforesiad Application now pending be-

fore the United States Atomic Energy Commission in Docket Nos. 50-416 and 50-417. On May 3, 1974, the Company was granted a Limited Work Authorization to begin site preparation for construction of the Grand Gulf Project. Petitioners anticipate receiving all necessary approvals from the Atomic Energy Commission in due course which will authorize not only site preparation work, but all other necessary construction and operating authority. That the Grand Gulf Project will, in all respects, meet the safety and environmental standards necessary for its construction, ownership and operation.

The proposed two 1250 MW generating units for the Grand Gulf Project will serve as a major source of base-load capacity for the Company and the entire Middle South System pooling arrangement. The proposed two units are necessary in order to provide capability with adequate reserves to Company and to the Middle South System to serve the projected electric loads of Western Mississippi and the entire area served by the Middle South System. Electric loads of Company and of the Middle South System have grown rapidly over the past years and are projected to continue this growth in the future. On the basis of load projections for the next ten years, it will be necessary for the Middle South Sysem, of which Company is a part, to add major units of generating capacity each year to maintain the capability required to carry the loads with adequate reserves. There is attached to the Joint Petition, as corrected by exhibits introduced in evidence at the hearing, marked Exhibit "E" and "F," respectively, and made a part thereof, tables showing thereon Company's and Middle South System's load and capability forecasts for the 10-year period 1973 through 1983. Said tables show that Units 1 and 2 of the Grand Gulf Project are necessary to prevent reserve capacities of Company and the Middle South System from dropping to dangerously low levels.

The minimum reserve margin for the Middle South System has been established at 16% based on operating experience over a long period of time. Thus, Unit No. 1 is necessary to meet the peak load season of 1980 in order to preserve the minimum reserve level of 16%.

By virtue of the fact that Company is a part of the Middle South System which is an integrated electric system, Company will have available for its customers such capability of the entire Middle South System as may be necessary for carrying Company's loads during the period of time reflected by the above schedules.

In order that Company may render adequate and dependable service to its customers and service areas pursuant to authority granted to Company by this Commission, it is necessary that Petitioners construct, own and operate the two units of the Grand Gulf Nuclear Station Project as proposed in the Joint Petition in this cause.

The proposed site of the Grand Gulf Project is a most favorable location electrically to supply the loads of Company's system and is centrally located in relation to the Middle South System. The river location is advantageous to the operation of said project. The location of the Grand Gulf Project affords maximum advantages consistent with safety and environmental factors concerning a nuclear station.

Units No. 1 and 2 of the Grand Gulf Project are estimated to cost in total approximately $1,227,000,000. It has been determined that it is economically and financially feasible to concentrate the financing and ownership of Middle South System's future base load generation in MSEI. Subject to receipt of appropriate approvals, Middle South Utilities, Inc. and MSEI will enter into a capital funds agreement, pursuant to which Middle South will

agree to supply or cause to be supplied such amounts of capital, in addition to (1) the capital made available to MSEI by Middle South as the purchase price of the common stock, and (ii) the amount to be made available under a bank loan agreement, as shall be required in order to complete the construction of the Grand Gulf Project, to permit the commercial operation of the steam electric generating units and to permit continued commercial operation over the expected life of the units. Subject to Securities and Exchange Commission approval, the money required for the construction, ownership and operation of the Grand Gulf Project will be supplied in part from cash generated through operation and in part from the sale, from time to time, of notes, debentures, bonds, preferred stock, common stock or any or all of them as required and as may be deemed appropriate in the light of MSEI's, Company's and Middle South's position and the market conditions prevailing at that time. Petitioners are financially able to construct, own and oeprate the Grand Gulf Project.

That Petitioners desire a Certificate of Public Convenience and Necessity from this Commission to permit Petitioners to construct, own and operate the aforesaid two units of the Grand Gulf Nuclear Electric Station Project, together with all component parts thereof, and related facilities necessary and required for the operation of same.

That the public convenience and necessity require that the two units of the Grand Gulf Project be constructed, owned and operated by Petitioners in the manner and form as set out in the Joint Petition and record of this cause in order for Company to meet the projected loads on Company's system and render adequate and dependable electric service to the customers and service areas of Company.

That although the general site of the generating plant is shown on exhibits to the Joint Petition, the actual location of said generating plant on the site will depend on ground surveys and terrain accessibility and nature of the area. That the construction of the aforesaid generating units should be approved, together with any additional land acquisitions that may be necessary, with the exact site of the generating units to be determined as above stated.

That Petitioners are ready, willing and able to construct, own and operate Units 1 and 2 of the Grand Gulf Project, all components necessary thereto and all related facilities, as applied for in the Joint Petition, and to operate the same and to render adequate electric service to all persons and premises which they may be legally entitled to serve. The present and future public convenience and necessity require and will require that Petitioners be granted by this Commission a Certificate of Public Convenience and Necessity to acquire, extend, construct, own and operate the Grand Gulf Project and related facilities as applied for in the Joint Petition filed in this cause.

IT IS, THEREFORE, CONSIDERED BY THE COMMISSION, ORDERED AND ADJUDGED, on hearing of said Joint Petition and all matters therein mentioned, that this Commission should, and by these presents, does hereby grant unto Mississippi Power & Light Company and Middle South Energy, Inc., the Petitioners herein, their successors and assigns, a Certificate that the present and future public convenience and necessity require, and will require, that Petitioners acquire the necesary property, easements, and rights of way and extend, acquire, construct, own and operate Units No. 1 and 2 of the Grand Gulf Project, together with all components necessary thereto and all related facilities, all as described and applied for in the Joint Petition filed in this cause on April

12, 1974, and to operate the same for the generation, transmission and distribution of electricity for intrastate sales to and for the public for compensation, as the same are fully described and applied for in the Joint Petition and as fully described in this Order.

IT IS FURTHER ORDERED by the Commission that Petitioners shall not by virtue of the aforesaid construction and this Order acquire any service area or additions to existing service areas.

IT IS FURTHER ORDERED by the Commission that this Order shall be effective from and after the date of its issuance.

The Commission retains jurisdiction of this matter for all purposes authorized by law.

ORDERED AND ADJUDGED on this, the 29th day of May, 1974.

/s/ E.W. Robinson
E.W. ROBINSON
EXECUTIVE SECRETARY

BENCH OPINION OF THE HONORABLE HENRY T. WINGATE, UNITED STATES DISTRICT JUDGE IN CIVIL ACTION NO. J87-0227(w) IN THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF MISSISSIPPI

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF MISSISSIPPI
JACKSON DIVISION

SYSTEM ENERGY RESOURCES, INC.

v. CIVIL ACTION NO. J87-0227(W)

MISSISSIPPI PUBLIC SERVICE COMMISSION; NIELSEN COCHRAN, COMMISSIONER, LYNN HAVENS; COMMISSIONER AND D.W. SNYDER, COMMISSIONER

BEFORE: The Honorable Henry T. Wingate, United States District Judge

DATE: May 16, 1987

PLACE: Jackson, Mississippi

APPEARANCES:

For the Plaintiff:

A. Spencer Gilbert, III
George Q. Evans

For the Defendant:

Crymes Pittman
Rick Wise
Joseph Roberts
Jesse Pendleton
Frank Spencer

For the Intervenor:

John K. Keyes

COLLEEN O'CONNOR
COURT REPORTER
Post Office Box 2202
Jackson, Mississippi 39225-2202

THE COURT: This dispute is now before the court on the plaintiff's motion for preliminary injunction in which System Energy Resources, Incorporated or SERI seek to enjoin the Mississippi Public Service Commission from further proceedings relative to cause No. U-4900 on the docket of the Mississippi Public Service Commission on the ground that the contemplated action of the Public Service Commission constitutes an unlawful infringement into an area governed exclusively by the Federal Energy Regulatory Commission or FERC.

On September 26, 1986, the Mississippi Public Service Commission entered an order establishing docket No. U-4900, the purpose of which was to investigate "The appropriateness of the rates and charges of Mississippi Power and Light Company and Middle South Energy, Incorporated," the latter having recently changed its name to System Energy Resources, Inc. or SERI. The proposed investigation consists of seven phases, the second of which proposes an audit of the books and records of Middle South Energy, Inc. or SERI pursuant to Mississippi Code Annotated Section 77-3-79, 1986. This statute enables the Public Service Commission to examine all accounts and records of state public utilities.

Notwithstanding this statute, SERI challenges the commission's authority to require SERI to open its records for inspection and audit. SERI claims that as a system operating company selling electricity in interstate commerce to its various utilities, it is under the exclusive jurisdiction of

the Federal Energy Regulatory Commission pursuant to the Federal Power Act Section 201 alpha, Title 16, United States Code, Section 824(A).

This exclusiveness argues SERI shelters it from contemplated actions such as these where the aim of the Public Service Commission is to intrude upon the setting of interstate rates which is wholly within the domain of FERC. Having heard arguments of the parties and having examined the briefs and authorities submitted by them, this court is now prepared to issue its ruling.

The burden of proof in this matter is on SERI to show that it is entitled to the extraordinary relief provided by the granting of a preliminary injunction by meeting four prerequisites set forth in the case of Canal Authority v. Callaway, 489 F.2d 567 (5th Cir. 1974). These four prerequisites are as follows. One, that there is a substantial likelihood the plaintiff will prevail on the merits. Two, there is a substantial threat that the plaintiff will suffer irreparable injury if the injunction is not granted. Three, that the threatened injury to the plaintiff outweighs the threatened harm the injunction may do to the defendant. And four, that granting the injunction will not disserve the public interest. In considering those four prerequisites the court must bear in mind that a preliminary injunction is an extraordinary and drastic remedy which should not be granted unless the party seeking such relief clearly carries the burden of persuasion.

SERI first argues that it is not a public utility under the Mississippi Public Utilities Act and thus is not subject to the orders of the commission. In support of this assertion, SERI cites two cases which hold certain particular services not to be public utilities. These two cases are Motorola Communications v. Mississippi Public Service Commission found at 515 F. Supp. 793 (S.D. Miss. 1979); and

Hinds County Water Company v. Scanlon, 132 So. 567 (Miss. 1931).

This court has reviewed these cases and find that they do not establish as a matter of law that SERI is not a public utility. In neither of these cases was the service in question ever issued a certificate of public convenience and necessity. Neither service had ever applied for a certificate and one was found by the court to be under the exclusive jurisdiction of the Federal Communications Commission. Furthermore, on April 12, 1974, Mississippi Power and Light Company and Middle South Energy, Inc. filed a joint petition seeking permission to be jointly engaged in the operation of equipment for the generation, transmission and distribution of electricity from the Grand Gulf Nuclear Electric Station project near Port Gibson, Mississippi. The petition asserted among other things that the Grand Gulf project falls "under the purview" of the Public Utilities Act of 1956 now found at Mississippi Code Annotated Section 77-3-1 ex sec Supplement, 1986. Specifically, the petition recited "That company is a utility as defined in Section 1(d)1 of the Public Utilities Act of 1956 Chapter 372 Mississippi Laws of 1956 as amended, Section 77-3-1 ex sec, Mississippi Code, 1972 hereinafter referred to as the act, that MSEI proposes to operate as a generating company owning, financing and operating electric generating facilities for the Middle South Utilities, Inc. system including the Grand Gulf project within the State of Mississippi. Therefore, the construction, acquisition, extension and operation of company facilities as well as its service areas and the proposed ownership and operation of the Grand Gulf project by MSEI fall under the purview of the aforesaid act".

SERI's next major argument is that the actions of the Public Service Commission are but a subterfuge to intrude

into interstate wholesale rate setting. The Public Service Commission denies this assertion and submits that its intentions are merely to exercise oversight jurisdiction of a public utility operating, operation which exists by virtue of a certificate issued by that commission. This court certainly recognizes that the FERC has exclusive jurisdiction over rates to be charged to interstate wholesale customers. Nantahala Power and Light Company v. Thornburg, 476 U.S., page unreported, 106 S.Ct. 2349 at 2357, 90 L.Ed 2d 943 (1986).

But this court certainly recognizes that the Federal Power Act is not intended to displace the states from areas of traditional regulation. Indeed, Section 301 of the Federal Power Act specifically states "Nothing in this act shall reliee any public utility from keeping any account, memoranda or records which such public utility may be required to keep by or under authority of the laws of any state". Clearly Section 301 was embodied to insure tht state commission shall not be precluded from prescribing accounting procedures necessary for their regulation. Appallachian Power Company v. FPC, 328 F.2d 237, Northern States Power Company v. Federal Power Commission, 118 F.2d 141 (7th Cir, 19741). In the latter case the court stated the system of accounting prescribed by the FERC does not preclude accounting regulation by the state body. The act plainly indicates the contrary.

The plenary authority then of the FERC over interstate rates does not bar the statutory authority of the Mississippi Public Service Commission to have access to and the right to inspect and examine all accounts, records, memoranda and property of SERI pursuant to Mississippi Code Annotated Section 77-3-79 Supplement, 1986 for whatever other proper purposes the Mississippi Public Service Commission may have. Therefore, SERI's refusal to allow the

Public Service Commission to audit its accounts and records is not justified on the basis of any exercise of unauthorized jurisdiction by the Mississippi Public Service Commission, nor can this court ascertain any deprivation of SERI's constitutional rights. The audit is clearly a proper exercise of state regulatory authority so long as it makes no attempt to interfere with the rate amounts mandated by FERC. Insofar as the audit is conducted to ascertain and clarify matters pertaining to the intrastate rates imposed by MP&L, it is reasonable and within the regulatory limits left to the states by congress.

Finally, SERI argues that it will be exposed to irreparable harm unless this injunction is granted specifically that its certificate of public necessity and convenience will be cancelled. This argument, however, depends upon a constitutional right of insulation from the scrutiny of the Public Service Commission which this court declines to find. Further, SERI may clearly avoid any suspension of its certificate by acquiescing to the audit by the Public Service Commission. Considering the legal arguments under the illumination cast by Canal Authority v. Callaway, this court finds that SERI has not met its burden of proof necessary for issuance of an injunction. *The defendants have argued equitable estoppel relative to SERI's denial of being a public utililty. This court is persuaded that the equitable estoppel argument is tenable in this case. Since SERI subjected itself to state regulatory authority in order to obtain its certificate, it cannot now claim that it was never subject to that authority.* (Emphasis supplied)

SERI is already subject to the jurisdiction of the Mississippi Public Service Commission and may avoid any suspension of its certificate by agreeing to allow its books to be audited. To impose an injunction upon the clear statutory authority of the state would work far greater hardship upon the public interest of the citizens of Mississippi so long as exercise of that authority has been shown to violate no federal law or constitutional right.

Finally, the public interest is often better served by scrutiny especially in matters having economic impact upon individual citizens. Adverse impact to the public due to an over charge, due to any over charges for electric power services is precisely what this form of scrutiny seeks to avoid. The public good cannot be served by enjoining the very process of public protection. Such an injunction requires a much stronger showing than has been made that SERI's rights have been violated or that the plenary authority of the Federal Government has been usurped.

It is therefore ordered that the motion for a temporary restraining order or other injunctive relief is hereby denied. The defendants are directed to prepare and submit an order to the court.

* * * * *

Excerpts from Cross Examination of
Donald C. Lutken, President and Chief Executive
Officer of Mississippi Power & Light Company
on June 3, 1981 in Cause #U-3967
Before the Mississippi Public Service Commission:
In Re Certificate of Public Convenience and Necessity
For Purchase of 25% of Independence Coal Plants

[BY ASSISTANT ATTORNEY GENERAL
FRANK SPENCER]

Q. Is this the latest Memo of Understanding regarding the allocation of capability down at Grand Gulf or is —

A. Yes, Sir.

Q. **Will the purchases of energy from Grand Gulf require the approval of the Mississippi Public Service Commission?**

A. **Yes, sir.** [Emphasis supplied]

Q. You told the Chairman that Arkansas is completely removed from participation in Grand Gulf at this time. What federal regulatory approval will MP&L seek or Mid South Energy seek to have Arkansas removed from that agreement?

A. We have to get the sale of the energy from the Grand Gulf nuclear station approved by FERC.

Q. Okay. My question really was Arkansas will not participate in Grand Gulf and it's my understanding that you must get the approval of some federal regulatory commissions before Arkansas can be totally removed from Grand Gulf transaction.

A. Well, I didn't mean to say that. I was trying to say is that the sale of energy has to be approved by the FERC energy and capacity to the owning companies. This is sort of like a, it's a wholesale transaction between the individual companies who are, will be purchasing from Grand Gulf.

Q. Do any federal regulatory commissions or entities have to approve Arkansas getting out of the Grand Gulf transaction?

A. No, sir.

Q. SEC, FERC?

A. As far as I know, no, sir. Maybe we can do some further research and find out, but as far as I know, no sir.

Q. Okay. All the companies have approved Arkansas not being in there?

A. Yes, sir. They signed this agreement.

* * * * *

Excerpts from Cross Examination of
Donald C. Lutken, President and Chief Executive
Officer of Mississippi Power & Light Company
on June 17, 1981 in Cause #U-3967
Before the Mississippi Public Service Commission:
In Re Certificate of Public Convenience and Necessity
For Purchase of 25% of Independence Coal Plants

BY VICE CHMN HAVENS:

Let me propose a question there. When you petitioned the Commission on Grand Gulf, didn't you petition for 19% ownership of Grand Gulf?

BY THE WITNESS:

I think we testified at that particular time we had not determined how it would be allocated and we said that our projected portion would be 19% —

BY VICE CHMN HAVENS:

But yet —

BY THE WITNESS:

—of our capacity responsibility.

BY VICE CHMN HAVENS:

But yet you've already signed agreement on Unit 1 for your share to be 33.6 and you haven't petitioned the Commission for any increase in that portion of Grand Gulf, have you?

BY THE WITNESS:

Well, what we did in the beginning was we petitioned this Commission —

BY VICE CHMN HAVENS:

But what I'm saying is, decisions are made — I'm getting the impression some decisions are made before petitions are filed.

BY THE WITNESS:

Well, that, we can make these decisions but what I think we're trying to say is this Commission has the final say-so as to what goes into MP&L's rate base, whether it be 19% of Grand Gulf or 33% of it.

BY VICE CHMN HAVENS:

How would you pay the difference between 19 and 33.6 if the Commission did not see fit to increase it?

BY THE WITNESS:

We couldn't. We'd just get 19% of it.

BY CMR SNYDER:

Who would get the other part?

BY THE WITNESS:

The other companies to their benefit.

BY MR. CHILD:

Mr. Lutken, let me ask you this just to clarify that point. Was not — was testimony at the Grand Gulf proceeding to the effect that there was an agreement in effect which fixed or measured MP&L's allocation of share, at that time?

BY THE WITNESS:

No, at that time I think I testified we would contemplate and had not been determined how they would be allocated, contemplated it could possibly be a participating unit and if it was our share would be at that time about 19% of it. Now we've gone and we've fixed the allocation of the plant and we have roughly some 34% of it and that agreement will stand, period, for the life of the plant.

* * * * *

Excerpts From Record of FERC Docket No. ER82-616-000 of Discussion of the Issues in the case Between FERC Administrative Law Judge Ernst Liebman and counsel for the various parties on March 14, 1983.

Transcript Pages 156-171

MR. EASTLAND: Your Honor, Mississippi Public Service Commission has a little additional light that we would like to shed on this particular allocation issue, and it is really twofold.

Our concern, first of all, goes with respect to the testimony which has been put in rebuttal by Middle South Energy, which they are attempting to drag into these proceedings a question under the guise of looking at the fixed allocation and whether or not it is just and reasonable or whether it has discriminatory aspects in setting the wholesale charge here.

They are attempting to also go further and look at whether or not it was actually prudent for MP&L to purchase that power, and I would like to explain it is our position –

PRESIDING JUDGE: For MP&L to purchase the power?

MR. EASTLAND: To actually purchase the power. It is our opinion that that is something entirely different. It is not appropriate for these proceedings, that these proceedings are here in order to set the wholesale charge, not whether the respective companies were prudent in making the purchases of that power.

We have a real problem with them bringing testimony into the record to that effect. It is not appropriate. It is not within the scope of the Federal Power Act as far as we are

concerned. It is not appropriate for this Commission to usurp the authority of state commissions with respect to retail impact on their customers, and this can have very significant impacts, which under the Federal Power Act, when it was enacted, decisions of this nature were left to the states.

I would like to explain that a little bit. Our second problem with respect –

PRESIDING JUDGE: Don't leave this first problem yet because I am not sure I understand it. Are you saying that MSE is arguing that under the allocation formula in the unit power sales agreement – is that what you call it?

MR. MERRIMAN: Unit power sales agreement.

PRESIDING JUDGE: – unit power sales agreement that they are arguing that the percentage allocation to –

MR. EASTLAND: That it was prudent for MP&L to purchase the power.

PRESIDING JUDGE: That it was prudent or imprudent?

MR. EASTLAND: They are arguing that it was prudent for them to do so. They are stating, your Honor, in the context of these proceedings, where in these proceedings the task here is to review with respect to this allocation issue whether or not this fixed allocation that they have set here is just and reasonable or whether it has discriminatory impacts due to things within this record or outside this record, if it is necessary to take certain other aspects into consideration, under the guise of questioning whether or not this fixed allocation is a proper method of distributing or equalizing the costs throughout the Middle South system with respect to the Grand Gulf power, under the guise of that review, justness and reasonableness and discrimination.

They are going a step further, and they are dragging into these proceedings an entirely different issue, not the justness and reasonableness of the wholesale charge.

They are walking around the table here and taking a look at whether or not the utility was prudent in purchasing that energy.

PRESIDING JUDGE: And they are saying it was prudent?

MR. EASTLAND: Correct.

PRESIDING JUDGE: Okay.

MR. EASTLAND: Prudent in purchasing that energy, I might add, for the purposes of utilizing that in retail sales. That is what, in our position, gets you within the scope of authority left to the states and the states' public service commissions.

It is our position that any testimony that they have submitted here with respect to the question of whether it was prudent for MP&L to purchase that power should be stricken from the record, as it is not appropriate.

We feel that this is well recognized by the state commissions, the federal courts, and FERC itself in various cases, wherein — in the context of wholesale proceedings where issues have come up, not with respect to whether or not the wholesale charge was just and reasonable or whether it had discriminatory impacts, but issues with respect to whether various parties were prudent in entering into those wholesale agreements.

And when this happens, the Commission has traditionally not imposed upon authority of the states to review whether it was prudent for these parties to enter into a transaction for the purpose of utilizing such power in retail sales.

That is our position.

PRESIDING JUDGE: Let me see if I understand your problem. Are you afraid of the determination by this Commission that the sales by MSE and the purchases by Mississippi Power & Light were prudent and therefore the state would be precluded from making some kind of an adjustment at the retail level?

MR. EASTLAND: I feel that is exactly what they are trying to do, your Honor.

PRESIDING JUDGE: That is what you are bothered by?

MR. EASTLAND: That is right.

PRESIDING JUDGE: Okay. Let me ask you this, though: doesn't the prudency question possibly go to the justness and reasonableness of the wholesale rate or the allocation?

For example, let me just throw a hypothetical at you. Suppose I decide that it was imprudent for Middle South Energy and the operating companies to negotiate an agreement which made the allocations of power and energy which the agreement makes and exclude Arkansas Power & Light, and therefore I conclude, suppose — suppose I conclude that those allocation percentages are unjust and unreasonable.

Now I am not saying the evidence will show that, but it seems to me I could do that. I could look at the prudency of what was done in respect to the rate setting that I have to do at the wholesale level without getting into the —

MR. EASTLAND: I agree.

PRESIDING JUDGE: — without getting into the retail level.

And what I think you are afraid of there is that a finding of prudency, if not worded properly, could be taken as a kind of res judicata or collateral estoppel for preemption.

MR. EASTLAND: Correct.

PRESIDING JUDGE: – at the state level.

MR. EASTLAND: That is right.

PRESIDING JUDGE: I think I understand the issue. Okay.

MR. EASTLAND: It is simply a matter – we are not saying that FERC is precluded from making determinations of whether it was prudent for the parties in the context of deciding whether it was the proper wholesale rate.

PRESIDING JUDGE: Okay.

MR. EASTLAND: We are concerned with a determination that would be so broad that it would be read as a FERC determination that it was prudent for MP&L to purchase this power, to utilize such power in retail sales. That is stepping on the toes of the state commissions in our position.

We think that it is inappropriate, not within the scope of these proceedings, and that any such testimony should be stricken.

The second aspect –

PRESIDING JUDGE: I haven't looked at the testimony with what you are saying in mind. Is it possible to do that kind of striking without striking testimony that is valid to the determination of the prudency question at the wholesale level?

MR. EASTLAND: It is possible we might run into a problem that some of the testimony there, that – this gets

me into my next problem here, but some of the testimony there may be with respect to the discrimination issue, but what we are asking is anything with respect to the actual prudence of MP&L purchasing it for retail sales – if it is in the context of purchasing it for retail sales.

I think I looked at Mr. Stampley's testimony where they are talking about the various representations that were made before the state commission to the retail commission. Things of that nature would obviously come up.

PRESIDING JUDGE: Well, let me take a look at what you want to strike, and if you can be fairly precise about that, and when we get to that testimony, we will deal with it.

MR. EASTLAND: Yes, sir.

MR. MERRIMAN: Do you want a comment from me?

PRESIDING JUDGE: Sure, I will take comments from anybody. I am trying to understand the issues and formulate them, and I would like to get them all "eared," because I think I explained earlier what I am going to do is enter an order which will define and look at the issues, and that will be it unless something comes up during the hearing and I am notified and all of the other parties are notified and we have revised the issue list in effect.

But I just want to be fair. I want everyone to know what we are shooting, and if we are going to shoot about some other things everyone should know about that, too.

MR. MERRIMAN: Well, I would just like to say this, your Honor. The unit power sale agreement is a contract on file as a rate schedule with this Commission, and our position is that our allocation is just and reasonable and proper and so forth.

And if it is, then obviously all of those that were involved in the transactions, including the seller and the purchaser, made prudent decisions, because if the allocation is proper, it is proper and it is just and reasonable and it is prudent.

We can't say that the seller made a good decision when you have this allocation, and we recognize that. We don't want to deny the state commissions or others any right to express their positions and views as they see fit.

But our position is this is the only forum that we can get these matters resolved involving the power sales agreement, and we have a purchaser and seller.

The contexts of all of the issues involving the power sale agreement are here before this Commission.

PRESIDING JUDGE: Let me ask a general question. Is anybody arguing that either the construction of the Grand Gulf plant or the actions of the parties – I mean the companies, the subsidiary companies, Middle South Utilities, in executing this unit power sales agreement were imprudent actions? Is there an imprudency argument here being made by anybody?

I understood that the Company put in some testimony about the prudency of the Grand Gulf project, which is perhaps a different issue. But is anybody saying that the entering into the agreement between MSE and the operating companies was an imprudent act, not that it is unjust and unreasonable and discriminatory but it is more than that, imprudent?

I do not read any of the pretrial briefs that way.

MR. FONTHAM: Your Honor, that is the problem. I think that is what Mississippi is raising here, and the difficulty is as follows. All of us think it is imprudent.

PRESIDING JUDGE: All of you think what is imprudent?

MR. FONTHAM: That it is imprudent for three of the operating companies who have executed agreements, placing upon themselves and their own ratepayers the costs of the Grand Gulf unit and allowing the fourth operating company –

PRESIDING JUDGE: So you are raising that imprudency issue.

MR. FONTHAM: Now, wait, all of us think it is imprudent. The question is whether the state commissions properly can be preempted by the fact that the company comes along and puts in 10 pages on prudency and so therefore place it in issue before your Honor and therefore arguably preclude the states from later on reviewing the question. That is the problem.

We have not placed it in issue here in the sense of the kind of a review that ordinarily would happen at the state level, which would be a really serious matter.

PRESIDING JUDGE: I cannot preclude the Company, MSE or any of the operating companies, from going before any state commission and saying our rates were approved by FERC as just and reasonable and nondiscriminatory, and therefore, argues one of these companies, they were prudent. I can't preclude them from doing that.

Now, the question is do I have to make a finding of prudence as well as a finding of justness and reasonableness and nondiscrimination.

And I don't think I have to get into the prudency question on that issue because my statutory standards, as I understand them, are what are the rates that are finally

prescribed by the Commission, initially by me, are just and reasonable and nondiscriminatory. And having found that, I don't have to go any farther, and I ordinarily would not.

So I don't see the prudency question arising. Even if a witness starts talking about it, I don't have to do that unless some of the Intervenors or Staff – and Staff are going to go farther and say not only is the agreement unjust and unreasonable for X, Y, and Z, but it is also unreasonable because it is imprudent.

Now if you raise that, then I do have to determine the prudency issue.

MR. EASTLAND: Your Honor, our position is prudency with respect to setting the wholesale rate charge and prudency with respect to whether they should have purchased that for retail sales. There are two totally separate questions there. And looking at the spheres of jurisdiction that exist for FERC and what is left to the states under the Federal Power Act, they are two different questions.

And when you come before the State Commission if there is a determination made here that these rates are just and reasonable and various distributions of cost, we're not even questioning the possibility of your reviewing in the context of just and reasonableness and what is discriminatory in the wholesale context, just the wholesale transaction and the wholesale charge, whether or not that's just and reasonable.

If that comes before the State Commission we recognize in Narragansett that we can't take apart your order and say that – and question your reasonableness determination. But what we say we can do is that you set a wholesale charge, it may have been a Rolls Royce that you set a price on, but it is not necessarily proper or prudent for that utility, for purposes of utilizing that power in retail sales, to buy that power.

That's what we're saying that we have the jurisdiction to make decisions with respect to.

PRESIDING JUDGE: Well, I wouldn't get into what the state would do at the retail level about the amount of power purchased, or whether the price was fair, or anything. I would only make a finding as to the justness and reasonableness of the agreement as finally modified, if at all, by me, and whether or not it is discriminatory. And I would not get into a prudency argument unless one of the Intervenors raises a prudency question.

I mean we have prudency questions in the gas cases now all over the place, with customers screaming that the purchasing practices of the pipelines were imprudent, and those prudency issues have been set for hearing in rate cases as an initial determination as to the justness and reasonableness of the rates and rate design, and what you should do if there is imprudence. So it comes into the justness and reasonableness.

But if you are not going to argue that – If the Intervenors themselves are not going to argue imprudence on behalf of the company, MSE or the operating companies, I'm not going to get into that issue.

MR. VINCE: Would your Honor be examining the issue of prudency in the subject of allocation?

PRESIDING JUDGE: Not unless you raise it.

MR. VINCE: Your Honor, New Orleans would concur then with the statements made earlier by Mr. Fontham, and we would perhaps propose to take this one step further and say that the allocation, first of all with reference to AP&L, was imprudent and secondly, with reference to

the individual operating companies was imprudent, and the methodology for the allocation was imprudent.

PRESIDING JUDGE: Okay. If you raise that question then I will have to decide the prudency issue in the context of deciding whether or not such alleged imprudency would justify a finding of unjust unreasonableness in the allocation or discrimination with respect to the allocation.

So you are raising the prudency issue?

MR. VINCE: With respect to allocation, yes.

PRESIDING JUDGE: Okay. So it's in.

MR. EASTLAND: Your Honor, within the scope of any prudency determination made here, we think it has previously been recognized by FERC in the Philadelphia Electric case, any prudency determination here. We're not saying that this Commission is precluded from making prudency determinations as those determinations impact on your decision as to justness and reasonableness with respect to wholesale rates. It's just a different matter with respect to retail.

The Philadelphia Electric case has language in there where an Intervenor, just as here, was advocating that they get into the prudency transaction there. For various reasons, they decided not to get into the prudency, but they pointed out that they by no means, in setting a rate, were precluding themselves in the wholesale context of examining prudency, and they specifically said "— or prejudge the state commissions on making prudency determinations in their separate jurisdictions."

MR. MERRIMAN: Your Honor, I'm familiar with the Philadelphia Electric case, and with all due respect, I read it differently, and I'm prepared — I don't think now is the time or the place but I'm prepared in brief to explain what

the Commission did in that case. It didn't set it for hearing. They accepted it as an initial rate for a limited period of time and said, "Since we're not going to get into a determination of just and reasonable, we're merely accepting it for filing, we're not going to pass on these matters."

Now we're prepared to argue that later on, but that order doesn't stand for what Mr. Eastland said it does, in our view. And he can argue his side and I can argue mine.

MR. EASTLAND: We're just saying, as one final statement here, if it's FERC's position in the State of Mississippi as well as the Mississippi Public Service Commission's to begin dictating terms with respect to prudency in retail sales, then I think we have very serious constitutional questions and we have serious questions as to whether that's within the scope or intent of the Federal Power Act.

PRESIDING JUDGE: I don't think I or the Commission would ever do that, in other words make a finding saying "Here are our determinations about prudency and they govern retail rates and everything else."

I think certainly my decision will be limited to the issues under Section 205 and 206, basically justness and reasonableness and discrimination in the agreement. And I will, since Counsel here is going to raise the prudency question on the allocation, I will have to get into it and decide whether or not there was indeed imprudence in entering into those kinds of allocations, but only so far as it deals with discrimination and justness and reasonableness.

MR. EASTLAND: Thank you.

* * * * *

Transcript Pages 245-248

PRESIDING JUDGE: Wait a minute. Let me just make sure we cover everything.

I am going to rule on justness and reasonableness of the allocation. If I find it is just and reasonable, that's it. If I find it is unjust and unreasonable, or is discriminatory, I will then make a just and reasonable and non-discriminatory allocation.

Now I suppose someone could argue that the unit sales agreement between MSE and the operating companies as purchasers was imprudently entered into by MSE and the companies, the operating companies, and therefore, the agreement is unjust and unreasonable and discriminatory.

And I think if someone raised that argument of prudency there as it goes to the justness and reasonableness and discrimination of the unit power sales agreement, I would rule on that. I would rule on that prudency issue. That's how I understand the prudency issue coming into the allocation issue.

MR. EASTLAND: Yes, Your Honor. And that's what I felt we covered this morning. That's with respect to setting the wholesale charge, not with respect to a retail jurisdiction.

PRESIDING JUDGE: But I may be doing more than setting a wholesale charge, is what I'm saying to you. I may reallocate the percentages of power and energy and costs among those companies, among the three or possibly among the four, depending on how I come out. And I might do that if someone makes the argument because there was imprudence in entering into this contract. It's just not from the point of view of MSE is what I'm saying to you.

MR. EASTLAND: And we're not covering anything though with respect to a particular company, the prudence of a particular company deciding to purchase?

PRESIDING JUDGE: I don't know about this. I don't know what testimony is coming into this prudency issue, or if anyone is really raising it, except New Orleans.

MR. VINCE: Yes, your Honor, New Orleans will raise that point.

PRESIDING JUDGE: There are five parties, as I understand it, to this agreement. Is that right? Or are there more? MSE and the four operating companies?

One, Arkansas Power and Light decided to take no entitlement, but still signed the agreement.

Bear in mind that under the Federal Power Act, I decide not only rates and charges but other things like conditions of service and things like that.

MR. O'SULLIVAN: But don't you decide them from the perspective of whether it is fair for the seller to propose them, not whether the buyer should have agreed to them?

PRESIDING JUDGE: Ultimately I will decide on — Well, no. You see, you're structuring it differently.

What I will come out with is a just and reasonable and non-discriminatory rate and tariff with conditions and everything else. That's what I will come out with.

MR. O'SULLIVAN: With Middle South Energy as the seller.

PRESIDING JUDGE: With Middle South Energy the seller, and the other people as buyers.

MR. MERRIMAN: How can you allocate power as a seller and not have buyers fund them? Your Honor, the answer to all of this is whatever happens is going to happen by operation of the law, hopefully. I hope you're going to do what you really ought to do in this case, and do it in a proper and fair manner. And then we'll go argue in State Court as to what effect that has.

PRESIDING JUDGE: I don't think you can put me in a position or this Commission in a position of deciding a prudency issue on the allocation issue in such a way that no one can possibly raise this in the State Court. I think that's the problem you have. I may be wrong.

I don't intend to get into state jurisdiciton, but I do intend to get into what a fair and just and reasonable and non-discriminatory rate schedule and agreement is.

MR. EASTLAND: Wholesale level.

PRESIDING JUDGE: At the wholesale level. Right.

And what somebody does with collateral estoppel or res judicata or something else in another forum, I have no control over.

Does that help?

MR. EASTLAND: Thank you, your Honor.

PRESIDING JUDGE: Okay.

May I read into the record the issues as I see them, and hope they come out tomorrow in the transcript the way we hope they ought to. And then we can talk about them and finalize them. And I'll do the best I can. I've got scattered notes here.

I'll read slowly.

The issues as I see them to be litigated in this case . . .

* * * * *

REPLY BRIEF

(10)

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

REPLY BRIEF IN SUPPORT OF JURISDICTIONAL STATEMENT

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi
39205
(601) 354-2385

Of Counsel:
WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 331-9400

Attorneys for Appellant

Counsel of Record

12 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Page

Statutes

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

**REPLY BRIEF IN SUPPORT OF
JURISDICTIONAL STATEMENT**

This is a reply to the Motions to Dismiss of the Attorney General of Mississippi ("Miss. AG") and the Mississippi Legal Services Coalition ("Miss. LSC") and to the Briefs *Amicus Curiae* of the Council of the City of New Orleans ("New Orleans") and the Arkansas Public Service Commission, Missouri Public Service Commission, and State of Arkansas ("Ark. PSC"). These filings confirm the importance of the question presented in this case. Upon analysis, they also underscore the point made by Justice Robertson of the Mississippi Supreme Court (J.S. App. 23a), by the amicus brief of the United States and the Federal Energy Regulatory Commission,[1] by the amicus brief of the Edison Elec-

[1]Brief for the United States and the Federal Energy Regulatory Commission as Amici Curiae, pp. 11-20 ("FERC").

tric Institute,[2] and by MP&L:[3] the federal question presented in this case is squarely controlled by *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986). Summary reversal would therefore be appropriate.

I. THE MISSISSIPPI SUPREME COURT'S DECISION IS A "FINAL JUDGMENT" UNDER 28 U.S.C. § 1257.

The arguments that the Mississippi Supreme Court's decision is not a "final judgment" ignore both the Mississippi Supreme Court's holding and settled law. Indeed, it is precisely because the judgment is clearly final that the Court has had to issue two separate orders staying the Mississippi Supreme Court's judgment.[4]

The federal question that Mississippi decided is whether MP&L has had a federal right to recover its FERC-allocated Grand Gulf 1 wholesale purchase power expense since the effective date of the FERC rate schedules that imposed those costs. The Mississippi Supreme Court has finally rejected this claim. It held that MP&L cannot begin recovering any of these expenses until after the Mississippi PSC makes its own independent determination of MP&L's "prudency" in incurring these expenses and that MP&L can thereafter recover only that portion of its Grand Gulf 1 expenses (if any) that the state commission finds to have been prudently incurred.[5] The Mississippi Supreme Court's holding thus required both a "roll-back" of MP&L's retail rates to exclude its Grand Gulf 1 expenses and an *immediate refund* of the more than $200 million in Grand Gulf 1 expenses that have been collected in retail rates pursuant to the Mississippi PSC order in the two years since the FERC rate schedules went into effect.

[2]Brief of Edison Electric Institute as *Amicus Curiae* in Support of Appellant's Jurisdictional Statement, pp. 9-16 ("EEI").

[3]Jurisdictional Statement, pp. 12-19 ("Jur. St.").

[4]On June 1, 1987, the Court stayed the Mississippi roll-back and refund orders, subject to the posting of a bond satisfactory to the Mississippi Supreme Court. On June 23, 1987, the Court stayed the Mississippi Supreme Court's subsequent order that prohibited MP&L from collecting or retaining revenues needed to recover Grand Gulf 1 expenses during the period in which MP&L and SERI were obtaining the regulatory and other approvals required for the posting of a bond.

[5]The Mississippi Attorney General states (Miss. AG, pp. 13-14) that the Mississippi PSC has not yet considered the question whether MP&L has experienced savings in other areas of its operation that offset some or all of the Grand Gulf 1 expenses and that this is a question on remand. However, as the Mississippi AG admits elsewhere in its motion (p. 8), the amount of " 'non-Grand Gulf' expense[s]" has been determined in an earlier order in the same docket. *See* J.S. App. 33a. The only issue in this appeal is whether MP&L has had the right to recover its Grand Gulf 1 expenses.

This appeal falls within at least two of the "four categories" in which a state court decision on a federal issue is a "final judgment," notwithstanding that "additional proceedings [are] anticipated in the lower state courts." *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 477 (1975).

First, this is a case in which the federal issue has been "finally decided by the highest court in the State," and "will survive and require decision regardless of the outcome of future state-court proceedings." *Id.* at 480. "[S]hort of settlement of the case," there is nothing that could or would "foreclose or make unnecessary" decision of the question whether MP&L has a federal right to retain the $200 million in Grand Gulf 1 wholesale purchase power expenses that it has already collected and to continue to collect those expenses. *Id.* Even if the Mississippi PSC were hereafter to determine that all the Grand Gulf 1 expenses were prudently incurred, that would, under the ruling of the Mississippi Supreme Court, only entitle MP&L to recover the expense from that day forward.

Ironically, the amicus curiae brief of New Orleans (pp. 16-17) recognizes the immediate, irreparable, and thus final impact of the Mississippi Supreme Court's judgment. New Orleans thus

proposes various devices by which this Court could purportedly prevent an immediate refund and "maintain the *status quo*" without deciding this case on the merits now. However, each proposal acknowledges that this Court *has* jurisdiction over this case now.

Second, *Cox Broadcasting* establishes that the Mississippi Supreme Court's decision would be a final judgment even if there were no refund and roll-back orders and even if the sole consequence of the decision were to require litigation of "prudency" before the Mississippi PSC. The Mississippi Supreme Court's holding will require years of litigation in a state tribunal on issues that, in MP&L's view, the Federal Power Act preempts a state commission from investigating or determining. As the Court has held, such preemption claims present "an issue separable from the merits and ripe for review." 420 U.S. at 483. Indeed, the Court has already applied this exception to the normal requirement of finality to exercise appellate jurisdiction under 28 U.S.C. § 1257 in a Federal Power Act case that is indistinguishable from the present case. *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-1307, 106 S. Ct. 3268 (June 23, 1986) ("*Nantahala III*"). *See* Jur. St., p. 2 n.2.[6] This Court's appellate jurisdiction is clear.

II. THIS CASE IS SQUARELY CONTROLLED BY *NANTAHALA*.

Appellees' and their amici's remaining arguments simply underscore that Mississippi is seeking to redetermine one of two

[6]Contrary to the Mississippi Attorney General's misstatement (p. 16), *Nantahala III* did *not* involve the FERC rate schedules at issue in *Nantahala I*, and the *Nantahala III* FERC rate schedules had not yet been approved by FERC. By noting probable jurisdiction and declining to dismiss the appeal, the Court recognized that it is a final judgment when a state supreme court decision rejects a claim of exclusive FERC jurisdiction, reverses a retail rate order that gives effect to a FERC rate schedule, and then remands for a determination of whether operating expenses incurred under a FERC rate schedule are reasonable.

matters that the Federal Power Act has assigned to FERC's exclusive jurisdiction and preempted states from determining: (1) whether SERI and the Middle South System as a whole acted "prudently" in planning, constructing, and completing Grand Gulf 1; and (2) whether it is "just and reasonable" for MP&L to be allocated 33% of the Grand Gulf 1 expenses and capacity. These are issues that must be, and have been, answered by FERC in proceedings in which all Mississippi parties appeared and presented their case.

The overriding fact is that a FERC determination that a wholesale rate is "just and reasonable" is, *a fortiori*, a determination that any underlying costs and investment of the utility (here, SERI) were "prudently" incurred. In arguing that the Middle South System's "prudence" in completing Grand Gulf 1 was nevertheless not at issue in the FERC wholesale rate proceeding, appellees and their amici rely exclusively on various statements of one of FERC's Administrative Law Judges from a pretrial conference. But these statements are quoted out of context. What the ALJ stated is that he "would not get into a prudency argument *unless one of the Intervenors raises a prudency question.*" Miss. Supp. App., p. 61 (emphasis added); *see also id.*, pp. 60-64.

The ALJ's statements reflect the fact that FERC presumes that the utility's underlying costs and investment were prudently incurred unless an intervenor makes a contrary claim and puts in evidence to support that position. *See* Jur. St., p. 7 n.5 (citing cases). More fundamentally, after SERI introduced evidence of its prudence in the FERC hearings, this ALJ made explicit findings that the completion of Grand Gulf 1 was "prudent." *See* Jur. St., p. 7 n.5. If the Mississippi parties and amici thought these findings were insufficient and applied an erroneous "legal test" (*compare* New Orleans, p. 8 n.4), their exclusive remedy was to challenge the ALJ's findings to FERC and, if necessary, on appeal to a court of appeals.

The fact that appellees and amici believe that state commissions are more receptive to "prudence claims" patently cannot authorize them to decline to litigate prudence issues that are within FERC's exclusive jurisdiction and then seek to raise the same issues in state forums on the theory that FERC has not decided them. *See, e.g., City of Tacoma* v. *Taxpayers of Tacoma*, 357 U.S. 320, 334-41 (1958). The Federal Power Act prohibits such forum shopping. Congress recognized that energy projects like Grand Gulf 1 are planned and built to serve a *multistate* area, and it enacted the Federal Power Act to assure that determinations of the reasonableness of the rates and of interstate cost allocations would be determined by a neutral federal agency, not by self-interested states. FERC's determinations that rate and power allocations are just and reasonable not only necessarily constitute findings that those rate and power allocations are prudent, but also preempt individual states from making different determinations.

Appellees and amici also argue that, at a minimum, Mississippi could examine MP&L's prudence in acquiring a 33% allocation of Grand Gulf 1 expenses and power when there are less expensive available power sources. They persist in arguing that this case presents the question that was reserved in *Nantahala* of whether the purchase of a particular *quantity* of power at a FERC-approved price can be deemed unreasonable when power is available at a lower price. FERC (pp. 16-18), EEI (p. 10), and MP&L (Jur. St., pp. 14-15) have previously demonstrated both the fallacy of this argument and that appellees' current claims are foreclosed by *Nantahala* itself. As the Mississippi Attorney General itself demonstrates (pp. 6-7, 21), the fact that MP&L had both low-cost and high-cost sources of power within the Middle South System was before FERC in FERC Opinions 234 and 234-A. Here, as in *Nantahala*, FERC determined the *quantity* of the low-cost and high-cost power that MP&L would be allocated and here, as in *Nantahala*, the Federal Power Act preempts the states

from concluding that MP&L acted "imprudently" in obtaining the capacity that FERC required it to purchase.[7] By the same token, FERC considered and rejected (J.S. App. 103a) the Mississippi Attorney General's "equitable estoppel" argument under which MP&L could be allocated no Grand Gulf 1 expenses until the 1990's, with those expenses to be borne by one or more other MSU operating companies (Miss. AG, pp. 26-29).[8] The court of appeals unanimously affirmed this action of FERC. *Mississippi Industries* v. *FERC*, 808 F.2d 1525, 1539-50 (D.C. Cir. 1987), *rehearing granted and vacated in part on other grounds*, No. 85-1611 (D.C. Cir. June 24, 1987).[9]

[7]Contrary to the Mississippi Attorney General's misstatements (Miss. AG, p. 14), the issue in *Nantahala* was the prudency of Nantahala's acquisition of high-cost power. There, the Court rejected the argument that North Carolina could disallow some of Nantahala's costs of acquiring "purchased power" from TVA (a transaction that FERC did not regulate) on the ground that Nantahala should have acquired more of the low-cost TVA "entitlements" power (a transaction that FERC did regulate) and thus needed less high-cost power. Because FERC had considered the pertinent power sources and allocated Nantahala a specified amount of the low-cost power, the Court held that Nantahala could not be said to have been "imprudent" in failing to secure more low-cost power. Slip op. at 14-15; 106 S. Ct. at 2358. This principle is dispositive here, particularly because MP&L participated in the FERC proceedings and sought to secure lower allocations for itself.

[8]As it did before FERC, the Mississippi Attorney General bases its equitable estoppel argument on an MP&L official's testimony in a Mississippi PSC proceeding that had nothing to do with Grand Gulf 1 and that occurred six years after the Mississippi PSC authorized construction of Grand Gulf 1. The short answer to this testimony is that no MP&L official can assure how FERC will exercise its authority over wholesale rates. Whereas MP&L sought to secure a lower allocation, FERC decided otherwise, and there is now no basis for Mississippi to overturn FERC's allocation by declaring that it is "imprudent" and therefore not "just and reasonable." If Mississippi could do so, so can Arkansas, Missouri, or Louisiana. This would nullify the Federal Power Act's careful plan for dual electric regulation.

[9]The amicus brief of the Arkansas PSC, *et al.* (pp. 3-10), argues that FERC somehow has no jurisdiction over the Grand Gulf 1 wholesale rates and cost allocations. This claim is not an issue in this case. Neither

(Footnote continued on next page)

In short, here, as in *Nantahala*, a state is collaterally attacking determinations that are expressly or impliedly made in FERC decisions and rate schedules and are embodied in a "filed rate." Under *Nantahala*, a state commission and other interested parties are entitled to participate in FERC proceedings to urge reductions in the filed rate (as all the Mississippi parties did here). But *Nantahala* holds that while the FERC-filed rate is in force, the state must give it effect and treat expenses incurred thereunder "as a reasonably incurred operating expense." Slip op. at 13; 106 S. Ct. at 2357. Thus, most of appellees' arguments (*e.g.*, Miss. LSC, pp. 12-14) reduce to claims that *Nantahala* (and its precursors that establish the "bright line" between state and federal authority) were incorrectly decided.[10]

(Footnote continued from previous page)
in the wholesale rate proceedings nor in their appeal to the Mississippi Supreme Court did either the Mississippi Attorney General or the Mississippi LSC challenge FERC's jurisdiction to allocate the Grand Gulf 1 costs at the wholesale level. Moreover, FERC's jurisdiction over wholesale rates may not be collaterally attacked in a state rate case. *See City of Tacoma* v. *Taxpayers of Tacoma*, 357 U.S. 320, 334-41 (1958). *See also Myers* v. *Bethlehem Shipbuilding Corp.*, 303 U.S. 41, 48-50 (1938). The exclusive means of challenging FERC's jurisdiction is by petition for review to the appropriate United States Court of Appeals. Whereas the Arkansas PSC has the right to raise this claim, whatever its merits, in a petition for certiorari to this Court—as, indeed it has (*see Arkansas Public Service Commission* v. *FERC*, No. 86-1380 (filed Feb. 20, 1987); *see also Arkansas Power & Light Co.* v. *FERC*, No. 86-1424 (filed March 4, 1987)), it may not inject this issue into this case.

[10] *Compare* Miss. LSC, pp. 12-14, *with FPC* v. *Southern California Edison Co.*, 376 U.S. 205, 215-16 (1964).

CONCLUSION

For the reasons stated, probable jurisdiction should be noted. Summary reversal would be appropriate.

Respectfully submitted,

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi 39205
(601) 354-2385

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 331-9400

Of Counsel:
WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

Attorneys for Appellant

August 25, 1987

**Counsel of Record*

AMICUS CURIAE

BRIEF

Supreme Court, U.S.
FILED
JUL 29 1987
JOSEPH F. SPANIOL, JR.
CLERK

(3)

No. 86-1970

In the Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
APPELLANT

v.

STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN,
ATTORNEY GENERAL OF MISSISSIPPI, and
MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

CHARLES FRIED
Solicitor General

LOUIS R. COHEN
Deputy Solicitor General

RICHARD J. LAZARUS
Assistant to the Solicitor General

Department of Justice
Washington, D.C. 20530
(202) 633-2217

CATHERINE C. COOK
General Counsel

JEROME M. FEIT
Solicitor

JOHN N. ESTES III
Attorney
Federal Energy Regulatory Commission
Washington, D.C. 20426

25 PH

QUESTION PRESENTED

Whether *Nantahala Power & Light Co.* v. *Thornburg*, No. 86-568 (June 17, 1986), requires a state public utility commission to allow an electric utility to recover, in retail rates, its share, as determined by the Federal Energy Regulatory Commission, of the costs of an electric power generating facility that supplies power to the utility and sister utilities in three other states.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

In the Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY, APPELLANT

v.

STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, and MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

INTEREST OF THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION

The Federal Power Act, 16 U.S.C. 791a *et seq.*, gives the Federal Energy Regulatory Commission (FERC) exclusive regulatory authority over the sale of electric energy at wholesale in interstate commerce. FERC is responsible for ensuring that all rates or charges made, demanded, or received by a public utility for or in connection with the transmission or sale of electric energy in interstate commerce are "just and reasonable" (16 U.S.C. 824d(a)). This case was preceded by a determination by FERC that the four operating companies in a public utility holding company system must share the costs of the holding company's investment in nuclear

power, in proportion to their relative demand for the energy generated by the system as a whole, by purchasing power from a particular plant in proportions specified by FERC. The Mississippi Supreme Court held in this case that the Mississippi state public utility commission may not allow the Mississippi operating company to raise its retail rates to recover its FERC-allocated share of the cost of purchasing this power unless the state commission first determines the "prudency" of that purchase. If allowed to stand, the Mississippi Supreme Court's decision would effectively nullify FERC's allocation of power and costs among the four companies. FERC participated as amicus curiae in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986), because the decision of the state supreme court in that case similarly threatened to nullify an exercise of FERC's exclusive statutory authority.

STATEMENT

In a FERC administrative proceeding in which the Mississippi Public Service Commission (MPSC) and the Mississippi Attorney General participated, FERC allocated the power and costs of a jointly planned nuclear power plant, Grand Gulf Unit No. 1 (Grand Gulf 1), among the four wholly owned electric utility subsidiaries of Middle South Utilities, Inc. (MSU): Mississippi Power & Light Company (MP&L), which operates in Mississippi, and three other utilities that operate in three other states. FERC concluded that its allocation would result in a just and reasonable sharing of the costs among the four companies. In a review proceeding in which MPSC and the Mississippi Attorney General again participated, the Court of Appeals for the District of Columbia Circuit affirmed FERC's determination that it had jurisdiction to determine the proportions in which the four companies shall bear these costs. In the present case, the Mississippi Supreme Court ruled that MPSC may not permit MP&L to increase its charges to retail customers in Mississippi, to reflect the Grand Gulf 1 costs allocated to MP&L by

FERC, "without first determining that the expenses were prudently incurred" (J.S. App. 2a).

A. The Middle South System And Grand Gulf Unit No. 1

Appellant MP&L is one of four operating electric utility companies that are wholly-owned subsidiaries of MSU, an integrated public utility holding company established in 1949 under Title I of the Public Utility Holding Company Act of 1935, 15 U.S.C. 79 *et seq.* The other subsidiary operating companies are Louisiana Power & Light Co., Arkansas Power & Light Co., and New Orleans Public Service, Inc. The four companies operate as a highly integrated power pool. They sell and exchange electricity at wholesale across state lines, to each other as well as to outside companies, and they also sell electricity at retail in separate service areas in four states. All capacity and energy on the Middle South system is centrally dispatched from the system's dispatch center at Pine Bluff, Arkansas. J.S. App. 3a-4a; *Middle South Services, Inc.*, 30 F.E.R.C. ¶ 63,030, at 65,141-65,142 (1985); *Middle South Energy, Inc.*, 26 F.E.R.C. ¶ 63,044, at 65,095 (1984).

In the late 1960s, the Middle South system sought to meet projected increases in demand and to diversify its fuel base (principally oil and gas) by adding coal and nuclear generating units. The Middle South system initiated the Grand Gulf nuclear power project in the early 1970s for these purposes. Under the original plan, MP&L would have been responsible for financing and constructing Grand Gulf 1, and New Orleans Public Service, Inc. (NOPSI), would have been responsible for financing and constructing Grand Gulf Unit No. 2 (Grand Gulf 2). Responsibility for construction of both units soon shifted to MP&L, however, because of siting problems within NOPSI's jurisdiction. When it subsequently became apparent that MP&L could not finance the construction, MSU made a system decision in 1974 to form a generation subsidiary, Middle South Energy (MSE) (now Systems Energy Re-

sources, Inc.), to finance the project. MSE acquired from MP&L all of its right, title, and interest in the Grand Gulf project. J.S. App. 118a.

By the late 1970s, it became evident that Grand Gulf's capacity would not be needed immediately to meet demand, which was lower than predicted in earlier forecasts. MSU continued to build Grand Gulf 1 on the assumption that the overall cost (fixed plus variable) per kilowatt hour would be less than that of alternative energy sources. The investment cost of Grand Gulf, however, continued to increase dramatically because of regulatory delay, additional construction requirements, inflation, and increased financing costs. As a result, although the investment cost of both Grand Gulf units had been projected to be $1.2 billion, the investment cost of Grand Gulf 1 alone was approximately $3 billion. The investment and other fixed costs associated with Grand Gulf 1 are substantially higher per kilowatt than the costs of other power generated by the MSU system (with the exception of one other nuclear plant). Although fuel costs are lower for Grand Gulf 1 than for most other system power sources, the overall cost per kilowatt hour is higher for Grand Gulf 1 than for other system sources. 30 F.E.R.C. at 65,144-65,145; 26 F.E.R.C. at 65,101-65,103; see J.S. App. 122a.[1]

B. Federal Proceedings

Under Part II of the Federal Power Act, 16 U.S.C. 824 *et seq.*, FERC has exclusive regulatory authority over the transmission of electric energy in interstate commerce and the wholesale sale of electric energy in interstate commerce. FERC is responsible for ensuring that all rates or charges, made, demanded, or received by any public utility for or in connection with the transmission

[1] Grand Gulf 2 has not commenced operation, and allocation of its costs is not at issue in this case.

or sale of electric energy in interstate commerce, as well as all rules, regulations, practices, and contracts affecting those rates or charges, are just and reasonable (16 U.S.C. 824(a)).

1. Transactions among the operating companies in the Middle South system have been governed by a series of "System Agreements" that must be filed with FERC. In 1982, MSU filed with FERC a 1982 System Agreement, which set forth the terms and conditions for transactions among the four operating companies (except the sale of power from Grand Gulf) and a Unit Power Sales Agreement (UPSA), which established wholesale rates for MSE's sale of power from Grand Gulf 1; the UPSA obliged Louisiana Power & Light, MP&L, and NOPSI, but not Arkansas Power & Light, to purchase specified amounts of its capacity and energy.

Pursuant to 16 U.S.C. 824d(a), FERC assigned the two contracts to two different administrative law judges to consider whether the contracts were "just and reasonable," as required by the Federal Power Act. MPSC and the Mississippi Attorney General participated in both administrative proceedings.

a. FERC reviewed the initial decisions of the two administrative law judges, rendered in February 1984 and February 1985,[2] and issued its decision in June 1985. *Middle South Energy, Inc.*, 31 F.E.R.C. ¶ 61,305 (J.S. App. 74a-152a), on reh'g, 32 F.E.R.C. ¶ 61,425 (J.S. App. 154a-195a), aff'd, *Mississippi Industries* v. *FERC*, 808 F.2d 1525 (1987), reh'g granted and vacated in part, No. 85-1611 (D.C. Cir. June 24, 1987) (Orders 1 & 2), petitions for cert. pending, Nos. 86-1380 & 86-1424. FERC concluded that the 1982 System Agreement and the UPSA would result in unjust and unreasonable allocations of costs between the operating companies and "that some form of equalization of nuclear plant costs is necessary to achieve just, reasonable, and non-discriminatory rates among the MSU operating companies" (J.S. App. 122a

[2] See *Middle South Services, Inc.*, 30 F.E.R.C. ¶ 63,030 (1985) (1982 System Agreement); *Middle South Energy, Inc.*, 26 F.E.R.C. ¶ 63,044 (1984) (UPSA).

(footnote omitted)). FERC determined, moreover, that the "most equitable allocation" would be for the operating companies to share in the system's total investment in nuclear capacity (four units, including Grand Gulf 1) "roughly in proportion to each company's share of System demand" (*id.* at 123a (footnote omitted)). On that basis, FERC ordered the following allocation of Grand Gulf 1 costs and power: Arkansas Power & Light, 36%; Louisiana Power & Light, 14%; MP&L, 33%; and NOPSI, 17% (*ibid.*).[3]

FERC's decision rested on two principal factual findings. First, FERC found that "the Middle South companies constitute a highly coordinated integrated electric system," which historically has "roughly equalized" generating costs among the four operating companies (J.S. App. 104a, 121a). FERC stressed that "this coordination and integration results in planning, construction, and operations which are conducted primarily for the system as a whole" (*id.* at 104a). FERC specifically found (*id.* at 115a-120a) that Grand Gulf had been planned "to meet MP&L's needs, to meet System needs, and to meet the System goal of diversifying fuel mix." Second, FERC found that Grand Gulf 1 was part of a reasonable system plan to diversify the fuel base by developing nuclear power to meet anticipated growth in demand (*id.* at 115a-126a).

FERC rejected contentions advanced by several parties, including MP&L, against the proposed allocation and in favor of other allocations more favorable to their interests. FERC rejected arguments by MPSC and the Mississippi Attorney General that the proposed allocation violated the doctrine of equitable estoppel because it was contrary to representations made by MP&L and MSE to MPSC, which MPSC relied upon in granting a certificate of public convenience and necessity to construct Grand Gulf 1 (J.S. App. 90a). According to FERC, "a State

[3] FERC's allocation of the "capacity" of Grand Gulf 1 includes a share of its power and its costs (both fixed capacity costs and variable energy costs).

[C]ommission could not reasonably rely on representations in State proceedings * * *, since [FERC] alone has jurisdiction over the [allocation issue]" and, in any event, "the doctrine cannot operate to bind [FERC] since [it] made no representations in and w[as] not a party to any of the State certification proceedings" (*id.* at 103a).

FERC also rejected a proposal of the Mississippi parties that the power and costs of Grand Gulf 1 be allocated instead under the terms of the 1973 System Agreement. FERC determined that allocation on that basis would be "inequitable and discriminatory because it would result in MP&L avoiding all responsibility for Grand Gulf for approximately 10 years, after which time it would enjoy the benefits of the project in the less expensive years" (J.S. App. 124a-125a n.19).

b. FERC subsequently clarified its June 1985 decision in the course of denying several petitions for rehearing (J.S. App. 154a-195a); FERC took that occasion to reject submissions that it lacked authority to reallocate the obligation to purchase Grand Gulf power and that FERC's allocation failed to consider the needs of individual operating companies (*id.* at 172a-192a). According to FERC (*id.* at 184a), when, as in the Middle South system, the operating companies "approach power planning on a system-wide basis, whereby the individual companies' needs are the component parts of the System power plan[,] [i]mplementation of the System plan * * * requires that the individual companies' needs be subsumed by the greater interests of the entire System." For this reason, FERC concluded, no one operating company could now avoid financial responsibility for Grand Gulf, which they jointly decided to build, finance, and allocate, as if the one company were an independent entity free to consider only its own immediate needs (*id.* at 157a; see 26 F.E.R.C. at 65,113).

2. On petition for review of FERC's orders, MPSC and the Mississippi Attorney General and parties from the other three states challenged FERC's jurisdiction to allocate Grand Gulf 1 power and costs and the allocation

FERC made. The Court of Appeals for the District of Columbia Circuit unanimously affirmed as to FERC's jurisdiction but ultimately vacated the allocation itself, remanding to FERC for a fuller explanation. *Mississippi Industries* v. *FERC*, 808 F.2d 1525 (1987), reh'g granted and vacated in part, No. 85-1611 (D.C. Cir. June 24, 1987) (Orders 1 & 2), petitions for cert. pending, Nos. 86-1380 & 86-1424.

a. Relying on this Court's decisions in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986), and *Pennsylvania Water & Power Co.* v. *FPC*, 343 U.S. 414, 422-423 (1952), the court of appeals upheld FERC's authority under the Federal Power Act to allocate the power and costs of Grand Gulf 1 (808 F.2d at 1539-1543). The court emphasized that "[a] consistent line of judicial precedent supports FERC's authority to approve and/or modify the terms of the pooling and coordination agreements of closely integrated power systems" (*id.* at 1~~545) and~~ that Grand Gulf 1 was "built and planned on a profoundly integrated basis" (*id.* at 1540).

The court of appeals, like FERC, specifically rejected the various objections raised by the Mississippi parties —MPSC, the Mississippi Attorney General, and Mississippi Legal Services Coalition—to FERC's allocation. The court agreed with FERC that there was no merit to their claim that the doctrine of equitable estoppel—based on prior representations by MSU and MP&L to the MPSC—limited FERC's reallocation authority (808 F.2d at 1549-1550). The court also concluded (*id.* at 1563-1565), with "little difficulty," that FERC had properly rejected the Mississippi's proposed allocation of the power and costs of Grand Gulf 1. Finally, the court rejected (*id.* at 1548) suggestions that the potential impact of FERC's allocation on retail rates required its invalidation.

b. The court of appeals initially affirmed, over Judge Bork's partial dissent, FERC's specific allocation of Grand Gulf capacity and energy (808 F.2d at 1553-

1566); subsequently, however, the court granted rehearing and vacated the portion of its judgment concerning the specific allocation, and the related portions of its opinion. See *Mississippi Industries* v. *FERC*, No. 85-1611 (D.C. Cir. June 24, 1987) (Order # 2); see 808 F.2d at 1568-1569 (Bork, J., dissenting). In accordance with Judge Bork's dissent, the court remanded the case to FERC "for reconsideration of the decision to equalize the capacity costs of all nuclear plants, and for an explanation of the criteria used to determine what constitutes 'undue discrimination' and of why [FERC's] ultimate decision is not unduly discriminatory" (Order # 2).[4]

C. Mississippi State Proceedings

1. Since Grand Gulf 1 went into service on July 1, 1985, MSE has billed the four operating companies, including MP&L, on a monthly basis in accordance with FERC's allocation. MP&L accordingly sought approval from MPSC to recover its Grand Gulf payments (about $27 million per month) in retail rates. MPSC granted full retail recovery of those costs but "phased in" the increase over a ten-year period, so that consumers would pay less than the full amount during an initial period and gradually pay the difference (plus financing charges) over a later period. J.S. App. 30a-31a.

2. On appeal by the Mississippi Attorney General, the Mississippi Supreme Court reversed (J.S. App. 2a-22a). The court ruled that under Mississippi law (Miss. Code Ann. § 77-2-39 (1972)) MPSC "must review the pru-

[4] On April 8, 1987, the panel had previously denied rehearing and the court of appeals had granted rehearing en banc to consider the terms of FERC's allocation (814 F.2d at 773). On June 24, 1987, the court of appeals issued two separate orders. In the first, the court, sitting en banc, vacated its prior order setting the case for rehearing en banc and reinstated the portions of the opinion and judgment it had earlier vacated. In the second, the panel vacated its earlier order denying the petitions for rehearing, granted the petitions, and reversed a portion of its opinion and judgment of January 6, 1987, concerning FERC's allocation. We have lodged copies of the two orders with the Clerk.

dency of an investment such as Grand Gulf before it can enact rates based on its cost" to "determine whether MP&L, MSE[,] and MSU acted reasonably when they constructed Grand Gulf 1, in light of the change in demand for electric power in this state and the sudden escalation of costs" (J.S. App. 19a-20a).

The state supreme court rejected (J.S. App. 14a-16a) MP&L's claim that MPSC was required, under *Nantahala*, to allow it to pass through the FERC-allocated costs of Grand Gulf in retail rates without undertaking any independent "prudency" review. According to the state court (J.S. App. 15a), MPSC would plainly have jurisdiction to consider "prudency" if MPSC had itself built Grand Gulf, and the court did not believe that the Supremacy Clause required a different result just "because Grand Gulf is owned by an out-of-state corporation." The court argued (*ibid.* (quoting *Nantahala*, slip op. 19) (emphasis omitted)) that *Nantahala* was not to the contrary because in *Nantahala* the Court had assumed "that a particular quantity of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere," but concluded that no lower-cost alternative was available in the circumstances of that particular case. The state court found (J.S. App. 15a (emphasis omitted)) that in this case, unlike *Nantahala*, "there is no doubt that Mississippians do not need the power provided by Grand Gulf, and that lower cost power is available elsewhere (in fact, by plants owned by MP&L)."

Finally, the state court concluded (J.S. App. 17a-18a) that preemption was inappropriate because FERC was never presented with, and never addressed, the question whether it was prudent to complete Grand Gulf 1 and continue its operation. The court stated (*id.* at 17a) that FERC had simply assumed that it was appropriate to complete construction of Grand Gulf 1, the D.C. Circuit had never addressed the issue in reviewing FERC's decision, and, as a result, the state court had "yet to

see MP&L, MSE[,] or MSU justify putting Grand Gulf on line at its exorbitant cost to ratepayers." [5]

Justice Robertson dissented (J.S. App. 23a). Relying on this Court's decision in *Nantahala*, he concluded that "our decision this day is in an area wholly preempted by authority granted by the Congress to [FERC]" (*ibid.*).

3. On remand, MPSC rescinded (J.S. App. 199a-200a) its September 16, 1985, rate increase and ordered MP&L to submit a plan for refunding all of its prior recovery of Grand Gulf 1 expenses from the retail ratepayers. On June 1, 1987, this Court granted a stay of the Mississippi Supreme Court's judgment conditioned upon MP&L posting a good and sufficient bond, in manner and amount to be determined by the Mississippi Supreme Court. On June 23, 1987, this Court granted a stay of the Mississippi Supreme Court's subsequent order that MP&L could not recover its Grand Gulf expenses until it had posted the required bond.

DISCUSSION

The decision of the Mississippi Supreme Court is flatly inconsistent with this Court's decision in *Nantahala*. In *Nantahala*, this Court affirmed the rule that "a state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred as a result

[5] The state court also ruled (J.S. App. 21a-22a) that MPSC must join MSU, the parent holding company, and MSE, the company that owns Grand Gulf 1, as parties in its review of the prudence of the Sales Agreement. In support, the court suggested an additional basis for its broader ruling that MPSC's authority had not been preempted by federal law. The court concluded that where, as in this case, agreements between the operating companies, including MP&L, were "suspect" because of the absence of arms-length bargaining, *Nantahala* requires only preemption of a state public utility commission's evaluation of a "FERC approved *rate*[]" (J.S. App. 21a (quoting *Nantahala* slip op. 12)); *Nantahala* did not, the court said, eliminate the state commission's jurisdiction to examine the "prudency" of the "suspect" agreements (J.S. App. 21a).

of paying a FERC-determined wholesale price" (slip op. 11). "[A] State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable" (*id.* at 13). In the FERC proceedings here, in which MPSC and the Mississippi Attorney General participated, FERC determined the wholesale price to be paid by MP&L for power it acquires: FERC ruled that MP&L, which draws all of its power from a variety of sources within the MSU system, should purchase 33% of the power of Grand Gulf 1. FERC's power to impose this obligation and associated costs on MP&L was squarely affirmed by the D.C. Circuit. The decision below, barring MP&L from passing the cost of purchasing its share of Grand Gulf 1 power on to its customers and therefore forcing that cost to be paid instead by its parent, MSU, or its sister utilities in other states, would, if allowed to stand, effectively nullify a FERC decision in which the State of Mississippi fully participated.

The Mississippi Supreme Court justified its conclusion on the ground that no one has authoritatively determined that it was "prudent" to build Grand Gulf 1 and that *Nantahala* leaves a state utility commission free to determine that the *quantity* of power procured from a particular source is excessive, because the utility's needs can be met from less expensive sources, even though the *price* of the higher cost power has been approved by FERC and must therefore be accepted as reasonable. But apart from the fact that the State of Mississippi issued a certificate of convenience and necessity and otherwise participated in the decision to build Grand Gulf 1, this argument is wrong for two reasons. First, the so-called "prudency" review traverses matters squarely within the exclusive jurisdiction of FERC. Second, this is a case like *Nantahala* itself, where all of the relevant sources of electric power are within the utility system and the sole question—one that only FERC can fairly resolve—is how the benefits and burdens of those sources should be shared between affiliated companies doing business in different states.

For these reasons we join appellant in urging further review by this Court. Because, moreover, the reasoning of the Mississippi court is plainly inconsistent with this Court's decision in *Nantahala*, we too believe that summary reversal would be appropriate.

1. FERC exercised its exclusive jurisdiction under the Federal Power Act to review the 1982 System Agreement and the UPSA filed by MSU. FERC determined that the terms of their allocation of Grand Gulf 1 were "unjust, unreasonable, unduly discriminatory [and] preferential." FERC accordingly exercised its remedial authority under Sections 205 and 206(a) of the Federal Power Act (16 U.S.C. 824d, 824e(a)) to determine and fix just and reasonable terms by ordering each of the four operating companies, including MP&L, to purchase an amount of Grand Gulf 1 power that would result in the companies sharing the costs of MSU's investment in nuclear generation in proportions based on their relative demand for energy on the system as a whole. On that basis, FERC allocated 33% of the power and costs of Grand Gulf 1 to MP&L. FERC's authority to *impose* just and reasonable obligations on the four companies was squarely affirmed by the D.C. Circuit in *Mississippi Industries* v. *FERC*, 808 F.2d at 1539-1543. The Mississippi parties—including MPSC, the Mississippi Attorney General, and Mississippi Legal Services Coalition—fully participated both in the FERC proceedings and in the review proceedings in the D.C. Circuit.

The Mississippi Supreme Court nevertheless concluded that MPSC could not allow MP&L to pass that FERC-allocated cost of purchasing power on to retail customers without first making its own inquiry into whether the cost was prudently incurred. The Mississippi Supreme Court apparently expects MPSC to consider either (1) whether Grand Gulf 1 was an imprudent undertaking for the Middle South system as a whole, so that some or all of its costs should be borne by MSU's shareholders rather than by the operating companies' ratepayers, or (2)

whether Grand Gulf 1 was imprudent for MP&L in some way that makes it appropriate for some or all of MP&L's share of the costs to be borne by the ratepayers of the other utilities in the other states. (There are no other possible sources of payment of MP&L's share.) But MPSC has no jurisdiction to consider either question.

First, MPSC has no jurisdiction to decide that Grand Gulf 1 was an imprudent undertaking for the Middle South system as a whole and that MSU and its shareholders must therefore bear some or all of its costs. The question whether MSU and its subsidiary MSE, which owns Grand Gulf 1, may charge the operating companies the full costs of Grand Gulf 1 as part of the price of the power that facility supplies to them is a question of the justness and reasonableness of the terms of interstate wholesale transactions in electric power, and it is within the exclusive jurisdiction of FERC. FERC had jurisdiction to consider the argument that Grand Gulf 1 costs were imprudently incurred and should not be passed through to operating utilities that are, for this purpose, its wholesale customers.[6] FERC determined that the full

[6] None of the parties, including those from Mississippi, argued before FERC that the costs of Grand Gulf 1 were not prudently incurred. FERC found (J.S. App. 115a-126a), moreover, that Grand Gulf 1 was part of a reasonable system plan to diversify the fuel base by developing nuclear power to meet anticipated growth in demand. FERC also explicitly affirmed and adopted (*id.* at 122a, 146a) the findings and conclusions of its administrative law judge who determined that MSU's decisions both to begin and to complete construction of Grand Gulf 1 were prudent (see 26 F.E.R.C. at 65,112-65,113). If FERC had instead found that those decisions were imprudent, FERC could have determined that it was not just and reasonable for MSU and MSE to charge the four operating utilities the full cost of Grand Gulf 1 power. In that circumstance, MSU's shareholders would have had to absorb those costs. See *New England Power Co.*, 31 F.E.R.C. ¶ 61,047, at 61,084 (1985), aff'd, 800 F.2d 280 (1st Cir. 1986). The Mississippi parties, however, made no such argument before FERC, FERC made no such finding, and the state public service commissions have no jurisdiction with respect to the issue.

costs should be borne by the operating companies in specified proportions, and "a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A state must rather give effect to Congress's desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority." *Nantahala*, slip op. 13.[7]

Second, MPSC has no jurisdiction to determine that Grand Gulf 1 was imprudent for MP&L in some way that makes it appropriate for more of the power and costs to be allocated to the three other utilities and their ratepayers. The allocation is the exact issue that FERC decided. FERC specifically rejected (J.S. App. 172a-192a), as did the D.C. Circuit in reviewing FERC's order (see 808 F.2d at 1547-1550), the contention that the needs of individual states should dictate an operating company's just and reasonable share of Grand Gulf 1. The D.C. Circuit expressly recognized (*id.* at 1548) that the direct consequence of FERC's allocation of power and costs to the four utilities would be corresponding increases in retail rates, and squarely upheld FERC's authority to bring about that consequence. The suggestion that an individual state public service commission may now revisit the allocation outside the federal administrative and judicial proceedings and, in effect, veto FERC's decision is flatly contradicted by the congressional decision to provide FERC with exclusive jurisdiction over

[7] The Mississippi Supreme Court asserted (J.S. App. 17a) that preemption was not warranted because "[s]everal aspects of prudency have never been addressed with respect to Grand Gulf, either by state or federal authorities." But " '[u]nder the filed rate doctrine, [FERC] alone is empowered to make that judgment [of reasonableness], and until it has done so, no rate other than the one on file may be charged.' " *Nantahala*, slip op. 10 (quoting *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 581-582 (1981) (brackets in original)). " '[T]he Supremacy Clause [does] not permit' " a state to " 'usurp[] a function that Congress has assigned to a federal regulatory body' " (*ibid.*).

these multistate controversies. As explained by the D.C. Circuit (*id.* at 1549 (citation and footnote omitted)), Congress concluded that FERC would be " 'in the best position to reach the most equitable result and to act in the public interest, rather than to be controlled by the necessarily parochial concerns of the States.' "

2. The Mississippi Supreme Court's attempt to distinguish this case from *Nantahala* is unavailing.[8] In *Nantahala*, this Court assumed arguendo "that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*" (slip op. 19 (emphasis in original)). In *Nantahala*, the Court concluded that no such inquiry could appropriately be undertaken by the state public utility commission because "[n]o [other] source of power * * * is said to be available * * *" (*ibid.*). In this case, the Mississippi court argues, MPSC may determine that the quantity of Grand Gulf power procured by MP&L was excessive. The problem, of course, is that the quantity of power to be allocated to MP&L is exactly what FERC determined.

This is not a case of the kind envisioned in the arguendo assumption in *Nantahala*, where a utility purchases power from an affiliate at a FERC-approved *price* while "lower-cost power is available *elsewhere*" (slip op. 19 (emphasis added)). Rather, this is a case like *Nantahala* itself, where all of the relevant sources of power, some of which are more expensive than others, are within the utility system and the sole question—one that only

[8] We do not believe that FERC's statements (J.S. App. 102a, 180a) in its federal administrative proceedings that "*Nantahala* is not directly on point" and "[t]he facts of *Nantahala* are clearly distinguishable from those here" suggest otherwise. Both statements occurred prior to this Court's decision in *Nantahala* and each referred to factual distinctions between these cases that are relevant only to a subsidiary legal issue and not to the issues in this case.

FERC can fairly resolve—is how the benefits and burdens of those sources should be shared between affiliated companies doing business in different states. FERC did not simply determine the reasonableness of the price of power from a particular source. Pursuant to its authority over wholesale transactions in interstate commerce, FERC determined that MP&L was obliged to bear the cost of purchasing a specified percentage of the power of Grand Gulf 1. FERC specifically rejected the alternative of MP&L's purchasing less or none of that power and relying instead on lower cost sources, such as the system power pool. Hence, to paraphrase *Nantahala* (slip op. 14-15), the Mississippi court's "assertion that [MP&L] should have obtained [less] of the [high]-cost, FERC-regulated power than [MP&L] is in fact [obliged] to claim under FERC's order * * * runs directly counter to FERC's order, and therefore cannot withstand the pre-emptive force of FERC's decision." Because MP&L is not free under FERC's order to avoid that obligation by seeking out a lower-cost source of power, MPSC (and the Mississippi courts) cannot deem MP&L imprudent for failing to do so.

The Mississippi Supreme Court's mistaken reliance on the arguendo assumption in *Nantahala* stems from the court's failure to apprehend the implications for MPSC's jurisdiction of MP&L's involvement in the Middle South system. The Mississippi court treated MP&L as though it were an independent, autonomous company. FERC, however, based its allocation of financial responsibility on its finding that MP&L and the three other operating companies are all wholly-owned subsidiaries of MSU, their operations are highly coordinated and integrated, and they were all deeply involved in every aspect of the planning of Grand Gulf, which they intended to serve the system as a whole (J.S. App. 104a, 113a, 181a). FERC found that because of those joint efforts, the operating companies must be held jointly responsible for Grand Gulf; contrary to the Mississippi court's assumption, they were

not, FERC found, autonomous companies that could opt out of sharing in the cost of Grand Gulf based on their own individual needs (*id.* at 184a-185a). See *id.* at 181a; 26 F.E.R.C. at 65,110-65,111, 65,113.

In this case therefore, as in *Nantahala* (slip op. 15), there is no occasion for a state public utility commission to "substitute its own conception of what allocation of * * * power would have been * * * fair" on the ground that the utility should have looked "elsewhere" for power. In both cases, FERC's allocation necessarily precluded the option of looking "elsewhere." [9]

3. The D.C. Circuit's recent decision (see pages 8, 9 and note 4, *supra*) to vacate FERC's order allocating the costs of Grand Gulf 1 and remand for further FERC consideration of certain issues does not diminish the importance or alter the proper outcome of this case. First, the court of appeals left intact most of its opinion and judgment, including its affirmance of FERC's exclusive jurisdiction over the allocation question. The remand requires FERC only to consider whether its specific allocation among the operating companies should be in somewhat different proportions; the fact that FERC will be revisiting the allocation of the costs of Grand Gulf 1 merely underscores MPSC's lack of jurisdiction to do so.

More important, the FERC allocation remains in effect until modified by FERC, imposing daily on MP&L costs

[9] The Mississippi court also suggested that MPSC "had the authority, indeed, the duty, to inquire into the prudency of the[] [UPSA and another FERC-filed system agreement]" because neither "fall[s] under the category of FERC approved rates" (J.S. App. 21a; see note 5, *supra*). The court argued that in the context of purchases by closely related entities *Nantahala* endorsed preemption only of state utility commission review of "'FERC approved *rates*'" (J.S. App. 21a (quoting *Nantahala*, slip op. 12)). *Nantahala*, however, supports no such limitation on the preemptive scope of FERC's allocation decisions. To the contrary, the Court expressly ruled (slip op. 13 (emphasis in original)) that "the filed rate doctrine is not limited to 'rates' *per se*." The statutory touchstone for FERC's jurisdiction is whether an agreement "affects" interstate wholesale rates (see 16 U.S.C. 824e(a)).

that must either be passed on to MP&L's retail customers or "trapped" (see *Nantahala*, slip op. 17). The decision of the D.C. Circuit reversed and remanded FERC's order establishing the allocation, but the filed rate containing that allocation is still in effect under the filed rate doctrine until changed by FERC,[10] and therefore must still be honored at the retail level under *Nantahala*. The possibility that FERC might, on remand, adjust its allocation of Grand Gulf 1 costs in a way that affects MP&L's share obviously does not justify disregarding FERC's decision in the interim.[11] Similarly, any question of refunds to MP&L for past Grand Gulf payments involves wholesale rates and hence is beyond the jurisdiction of MPSC. Of course, should MP&L receive refunds for its Grand Gulf 1 payments at any stage, MPSC can, as it recognized when it initially granted MP&L partial rate relief in this case (see J.S. App. 51a), require that those refunds be passed through to retail ratepayers.

[10] See *System Energy Resources, Inc.*, 40 F.E.R.C. ¶ 61,078 (1987); see also *Burlington Northern, Inc.* v. *United States*, 459 U.S. 131, 141 (1982) ("federal-court authority to reject Commission rate orders for whatever reason extends to the orders alone, and not to the rates themselves").

[11] Nor is there any realistic possibility that the outcome on remand will moot this case or reduce its importance. The issues to be considered on remand do not suggest the possibility that FERC will adopt an allocation under which MP&L's share of Grand Gulf costs is very small or zero.

AMICUS CURIAE

BRIEF

(5)

No. 86-1970

In the

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI, *ex rel.* EDWIN LLOYD PITTMAN, ATTORNEY GENERAL and THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

Brief of Edison Electric Institute as *Amicus Curiae* in Support of Appellant's Jurisdictional Statement

JAMES B. LIBERMAN
Counsel of Record
Berlack, Israels & Liberman
1155 Avenue of the Americas
New York, NY 10036
(212) 704-0100
Attorneys for Edison Electric Institute

Of Counsel:
ROBERT L. BAUM
Senior Vice President
and General Counsel
Edison Electric Institute
1111 19th Street, N.W.
Washington, D.C. 20036
(202) 778-6500

August 10, 1987

1988

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

In the

Supreme Court of the United States

OCTOBER TERM, 1986

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI, *ex rel.* EDWIN LLOYD PITTMAN, ATTORNEY GENERAL and THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

Brief of Edison Electric Institute as *Amicus Curiae* in Support of Appellant's Jurisdictional Statement

Interest of *Amicus Curiae* Edison Electric Institute

Edison Electric Institute ("EEI") is the nation's association of investor-owned electric utilities. The members of EEI supply electric service to consumers throughout the United States, serving approximately 97 percent of all customers of investor-owned utilities and 73 percent of this country's electricity users.

Electricity is more than a convenience—it is a necessity for everyday life and commerce. Increasingly, the ability to provide this critical resource on a reliable and economic basis rests upon an array of wholesale for resale and transmission power transactions among EEI's members. In large part, these transactions take place pursuant to the terms of power pooling or other highly integrated contractual or corporate arrangements.[1] These wholesale flows of power

[1] Appellant, Mississippi Power & Light Company ("MP&L"), and its operating utility affiliates, Arkansas Power & Light

(*footnote continued on following page*)

extend across every state border in the continental United States, and provide enormous benefits to power consumers.[2]

The establishment and maintenance of a reliable network of power generation, transmission, and distribution facilities to carry out these arrangements is a task that is national in scope and consequence. As this case demonstrates, the events of the past two decades, mostly national in origin and consequences, have placed great stress on the financing and operation of that network and on the pricing of the services which it provides. Examples of those national events include the rapid inflation of construction and financing costs for major capital projects, the federal government's initiative for the construction of nuclear projects, the dramatic fluctuations in the availability and prices of oil and gas, the governmental and non-governmental efforts to shift from oil-fired and gas-fired electric generation to nuclear and coal-fired electric generation in response to the Arab oil embargo and OPEC pricing actions, the related federal legislation precluding for a time continued reliance upon natural gas for electric generation (see, *e.g.*, the Power Plant and Industrial Fuel Use Act of 1978, 42 U.S.C. § 8301 *et seq.*), the changes in regulatory requirements following the 1979 Three Mile Island accident and the resulting increases in construction and operating costs, and the roller-coaster rapid surges and declines in electric load growth forecasts and usage.

(*footnote continued from preceding page*)

Company, Louisiana Power & Light Company, New Orleans Public Service, Inc., System Energy Resources, Inc., formerly known as Middle South Energy, Inc. ("MSE"), the owner of a 90% interest in Grand Gulf Station Unit No. 1 which is the subject of this proceeding, and their common parent, Middle South Utilities, Inc. ("MSU"), constitute "a highly integrated and coordinated electric utility system" (R.104a) and are members of EEI.

[2] The Department of Energy's Report, dated March 1987, to the President entitled "Energy Security", states (at 158) that wholesale power transactions have grown by 40% and wheeling by 150% over the past 10 years, while retail sales have grown by only 30%.

The consequence of these national developments has been that nuclear generating capacity placed in service in 1985 (such as the Grand Gulf nuclear generating station which is at the center of this litigation) had an installed cost on the order of $2,500 per kilowatt (see *Mississippi Industries v. F.E.R.C.*, 808 F.2d 1525, 1532 (D.C. Cir., 1987), or approximately five times that of nuclear generating capacity placed in service by one of MP&L's affiliates, Arkansas Power & Light Company, only a few years earlier. This phenomenon is not unique to Grand Gulf or the Middle South System.[3] Moreover, this same disparity in investment cost of new facilities as against that of older facilities is also applicable to coal-fired generation and transmission facilities, although it is less severe in degree.

It is not surprising—although it is disappointing in light of the prior decisions of this Court—that, under these circumstances, the Supreme Court of one state should (as in this case) refuse to recognize the controlling effect of FERC's allocation of the costs of a facility providing electric service to the citizens of several states, and, instead, disallow recovery in retail rates of its state's allocated share of such costs.

The allocations of costs of a large generating plant or transmission network serving the electric energy needs of customers in several states pursuant to a power pool or other highly integrated contractual or corporate arrangement present issues that in many instances can be resolved only by a neutral federal arbitrator. The rate and other conditions affecting such interstate wholesale power sale and transmission transactions are, therefore, required to be administered exclusively by FERC pursuant to the Federal Power

[3] A report of the Energy Information Administration of the Department of Energy entitled "Nuclear Power Plant Construction Activity 1985" states (at page 13) that seven nuclear units entered commercial service in 1985 with an average construction cost of $2,466 per kilowatt and that, for nuclear units expected to enter commercial operation in 1986, the average estimated cost is $3,230 per kilowatt.

Act. As recently as the close of its last term, this Court emphasized the need to give effect to the preemptive consequences of federal determinations relating to these interstate power operations. *Nantahala Power & Light Co. v. Thornburg*, 106 S. Ct. 2349 (June 17, 1986).

When a utility's costs are "trapped" by conflicting retail and wholesale rate orders, the utility suffers immediate financial repercussions. Its cash flow is disrupted, and its ability to make needed purchases of fuel or power and to finance additional capital expenditures is diminished. As in this case, such orders quickly precipitate grave financial crises and threaten to interrupt the operation of wholesale power transactions affecting utilities in several states. An EEI member serving customers in one state that relies upon generating or transmission facilities serving retail customers in different states may also find the financial viability of the entire project endangered by the retail rate actions of a commission of another state.

The adverse effects of such financial distress are felt not only by investors in the utility's securities, but by the utility's customers as well, because the company's ability to attract capital and operate on a least-cost basis is impaired. Moreover, such trapping of costs undercuts the commercial certainty required to support wholesale bulk power transactions, interstate interconnections and pooling arrangements. Such transactions and arrangements achieve substantial efficiencies and thus increase the interstate availability of economic and reliable electrical energy.

Part II of the Federal Power Act, 16 U.S.C. § 824 *et seq.*, was enacted in response to the determinations of this Court of the limitation of state authority in the regulation of interstate commerce in electricity. *Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927). The distinction between state and federal jurisdiction under that Act was to be a "bright line," making FERC jurisdiction plenary and extending it to all wholesale

sales in interstate commerce except those which Congress has made explicitly subject to regulation by the states. *FPC v. Southern Cal. Edison Co.*, 376 U.S. 205, 215 (1964); *Arkansas Electric Coop. v. Arkansas Public Service Commission*, 461 U.S. 375, 379-80 (1983). That "bright line" is in danger of being obliterated by repeated refusals of state commission (and state appellate court) members to accept the Supremacy Clause of Article VI of the Constitution as binding upon them individually. A prompt reminder by this Court that its decisions in *Nantahala* and other cases cited are controlling in the circumstances here presented would be significant to all of EEI's members, to the millions of customers whom they serve, and to the millions of investors in their securities.

Statement of the Case

EEI adopts the Appellant's Statement of the Case in its Jurisdictional Statement as augmented for subsequent developments by the Brief, dated July 1987, for the United States and the Federal Energy Regulatory Commission as *Amici Curiae*.

Reasons Why the Court Should Note Probable Jurisdiction and Summarily Reverse.

1. There is no merit in the Mississippi Supreme Court's argument that this Court's decision in *Nantalaha* is not controlling in this case.

As Appellant has stated in its Jurisdictional Statement,

> [t]he question presented in this case is not only substantial; it is indistinguishable from the issue decided last term in *Nantahala Power & Light Company v. Thornburg*, No. 85-568, 106 S.Ct. 2349 (June 17, 1986).

In *Nantahala*, this Court held that an allocation of "entitlement power" prescribed by FERC in determining a utility's wholesale rates must be given binding effect by the state commission in determining that utility's retail rates. Therefore, the state utility commission's retail rate determination, which was based on a different allocation of "entitlement power", was held to be preempted under the Supremacy Clause by the rate filed with the FERC under Part II of the Federal Power Act (FPA). Accord, *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (1951); *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981).

In reaching its decision in *Nantahala*, this Court approved a body of state court precedent concluding that a state utility commission setting retail rates must allow, as reasonable operating expenses, costs incurred as a result of paying a wholesale rate filed with or approved by the FERC under the FPA, including one case decided by the Mississippi Supreme Court itself, *United Gas Corp. v. Mississippi Public Service Comm'n*, 240 Miss. 405, 127 So.2d 404 (1961). *See also*, *Narragansett Electric Co. v. Burke*, 381 A.2d 1358 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1978). A preemptive effect attaches to such filed rates in order to preserve FERC's exclusive jurisdiction under the FPA to regulate interstate wholesale rates and arrangements. Otherwise, as *Nantahala* explains

(106 S.Ct. at 2359) a utility's wholesale costs could be "trapped" between the FERC-filed rates the utility must pay, and the state's disallowance of such costs from recovery in retail rates. The decision of the Mississippi Supreme Court catches MP&L's wholesale costs for Grand Gulf power in the trap *Nantahala* condemned. Unless and until the rate schedules allocating Grand Gulf costs) filed in compliance with FERC's decision are modified, they constitute preemptive filed rates which the Supremacy Clause, as applied in *Nantahala*, requires Mississippi's tribunals to recognize.[5]

The Grand Gulf plant became operational on July 1, 1985. The Middle South companies filed the tariffs to implement the FERC 1985 decision and began collecting

[5] In *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987), rehearing granted and vacated in part D.C. Cir. No. 85-1611, June 24, 1987, the D.C. Circuit unanimously held that FERC's allocation of Grand Gulf costs was within its authority under §§ 205 and 206 of the Federal Power Act to remedy discrimination. In its order of June 24, 1987, granting rehearing, the D.C. Circuit reversed FERC's determination on the merits and remanded for reconsideration FERC's decision to equalize the capacity costs of all nuclear plants in the Middle South system and for an explanation of two other factors. On July 24, 1987, FERC entered an order providing for further proceedings on remand. That order made clear, however, that the rates filed in compliance with FERC's 1985 allocation remain in effect until further action by the Commission on remand:

> The rates currently on file reflect the allocation ordered by the Commission in Opinion No. 234. No other rates being on file or in effect, the rates filed in compliance with Opinion No. 234 remain in effect. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981); *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (1951); *see also Burlington Northern Inc. v. United States*, 459 U.S. 131, 141 (1982) ("federal court authority to reject Commission rate orders for whatever reason extends to the orders alone, and not to the rates themselves").

Thus, under the filed rate doctrine, Mississippi tribunals must continue to recognize the current allocation reflected in those rates until they are modified on remand or otherwise as provided in the Federal Power Act.

from MP&L as of July 1, 1985 the amounts called for by such tariffs. Those tariffs are still in effect.[6] Under the filed rate doctrine MSE and MP&L would violate the Federal Power Act if MSE had not collected from MP&L amounts pursuant to the tariffs prescribed by FERC and in effect since July 1, 1985.

The decision of the Supreme Court of Mississippi in this case is a collateral attack on the FERC orders allocating Grand Gulf costs. Those FERC orders were the result of extensive proceedings before the FERC with respect to two agreements among the members of the Middle South System that had been filed with the FERC in 1982. The state public utility commissions, local regulatory agencies, and other public authorities in each jurisdiction served by the Middle South companies (including those in Mississippi) intervened and participated in the FERC proceedings. Each urged a different allocation of Grand Gulf costs. As FERC noted in its June 1985 Order (R-78a),

> . . . despite every encouragement and opportunity, the parties were unable to unanimously resolve their differences.

Thus, FERC was required to serve as the arbiter of the conflicting interstate interests,[7] and to prescribe the allocation

---

[6] See n.5 *supra.*

[7] In dealing with a comparable challenge by the Public Service Commission of West Virginia to a FERC allocation of the costs burdens of an interstate energy transmission network, the Court of Appeals for the Fourth Circuit recently stated:

> Only FERC, as a central regulatory body, can make the comprehensive public interest determination contemplated by the FPA and achieve the coordinated approach to regulation found necessary in [*Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1972).] . . . . Only FERC has the objectivity and comprehensive overview that transcends these local concerns. *Appalachian Power v. PSC of West Virginia*, 812 F.2d 898, 905 (4th Cir. 1987).

which determined the share of Grand Gulf costs each state would bear. Because the rates reflecting that allocation remain in effect as the only rates on file, *Nantahala* is controlling.

In *Nantahala*, two owners (both subsidiaries of Aluminum Company of America), Nantahala and Tapoco, of a number of hydroelectric projects made available to the Tennessee Valley Authority ("TVA") the output of those projects in return for a constant allocation of low-cost TVA "entitlement power" and the opportunity to buy from TVA more expensive "purchased power." The agreements allocating these two types of TVA power were filed under the FPA. The FERC determined that the allocations between Nantahala and Tapaco should be modified so as to increase modestly the quantity of entitlement power available to Nantahala and directed Nantahala to file with the FERC revised rates to give effect to that decision. Nantahala did so.

The North Carolina Utilities Commission ("NCUC") had contended before the FERC that the FERC should treat Nantahala and Tapoco as a single entity and should allocate the TVA power allocations on that basis, which would have reduced Nantahala's total cost for TVA power substantially more than that resulting from the FERC order. FERC did not do this, because, given the particular history of Tapoco and Nantahala, FERC concluded that it could not find that Tapoco and Nantahala "operate[d] as an integrated system" (*Nantahala*, 106 S.Ct. at 2352).

Nevertheless, NCUC fixed rates for Nantahala's sales to its retail customers on a basis which attributed to Nantahala more low cost "entitlement power" and less higher-cost "purchased power" from TVA than FERC had directed. The North Carolina Supreme Court affirmed the NCUC's action.

On appeal, this Court reversed the North Carolina Supreme Court's decision, holding that the FERC's determination of the allocation to Nanhatala of low-cost entitlement power

was preemptive and that the NCUC's action impermissibly interfered with federal regulation under the FPA.

The basis for federal preemption in this MP&L case is even stronger than in *Nantahala*. After detailed examination, FERC concluded that the Middle South System is a highly integrated system that made critical decisions as a unit and that the allocation of Grand Gulf costs should take that fact into account.

The Mississippi Court's reliance upon the following statement from this Court's opinion in *Nantahala* (106 S.Ct. at 2360) is misplaced:

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*. (emphasis in original)

But that assumption *arguendo* in *Nantahala* has no applicability here. MP&L did not simply *elect* to purchase the 33% share of Grand Gulf power allocated to it by FERC. Initially, in the Unit Power Sales Agreement ("UPSA") the Middle South companies sought to provide an allocation among themselves of the cost burdens of Grand Gulf which they believed to be appropriate. After extensive and hotly contested proceedings with participation of all interested parties, FERC made a determination allocating the Grand Gulf cost burdens (and associated power entitlements) in the shares which it concluded were most equitable in the light of all the circumstances. That FERC determination increased MP&L's share of Grand Gulf costs modestly to 33% and significantly changed the shares of such costs of the other Middle South operating companies. MP&L has no choice but to bear 33% of the Grand Gulf costs so long as the present MSE tariffs directed by FERC remain in effect—*i.e.*,

the quantity and price of Grand Gulf power to be purchased by MP&L are exactly what FERC directed.

2. The Mississippi Supreme Court's characterization of its decision as not challenging FERC's jurisdiction over interstate rates is far wide of the mark.

FERC's decision stated (R-101a):

> . . . the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent. In other words, the real issue is whether rates among those companies are just, reasonable, and not unduly discriminatory.

Presumably because it recognized that an attempt on its part to do so would have been in blatant disregard of *Nantahala*, the Mississippi Court never explicitly addressed that "real issue" of "whether rates among those [Middle South] companies are just, reasonable, and not unduly discriminatory".[8] But, even though the Mississippi Court stated (R-14a-15a) "we do not challenge FERC's jurisdiction over interstate wholesale rates", the whole of the Mississippi Court's decision is precisely such a challenge—*i.e.*, the Mississippi Court flatly refuses to accept as binding the Grand Gulf costs allocated to MP&L by FERC.

Moreover, FERC's decision rests in significant part on its conclusion that the Middle South companies constitute a highly coordinated integrated system and that this coordination and integration result in planning, construction and operations which are conducted primarily for the system as a whole (R-104a). But it is precisely those elements of integrated

[8] The "bright line" Congress drew in the Federal Power Act preempts the states from deciding issues over which FERC has asserted its exclusive jurisdiction. See, *e.g.*, *Arkansas, Louisiana Gas Co. v. Hall*, 453 U.S. 571, 580-582 (1981); *Arkansas Electric Coop. v. APSC*, 461 U.S. 375, 379-380 (1983); *FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964).

and coordinated operation and those affiliated relationships that are seized upon by the Mississippi Court (R-16a; R-20a) as justification for its apparent position that the FERC decision allocating Grand Gulf costs may be ignored by the MPSC in determining MP&L's retail rates. Consequently, the Mississippi Court not only challenges the exercise of jurisdiction by FERC, but also the rationale employed by FERC in reaching its conclusion. Both challenges are without merit.

In a similar vein, the Mississippi Court stated that the Unit Power Sales Agreement ("UPSA") (which provides for the sale of Grand Gulf capacity and energy by MSE to three of the Middle South operating companies) does not "fall under the category of FERC approved rates" (R.21a).[9] This bald assertion is simply wrong, as well as directly contrary to the holdings of FERC and the D.C. Circuit that the Grand Gulf UPSA involves rates for the sale for resale of electricity in interstate commerce under the Federal Power Act.

FERC's jurisdiction over the matters here involved is based on Section 206 of the Federal Power Act which provides that, when any rule, regulation, practice or contract affecting a rate, charge or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice or contract to be thereafter observed and in force and shall fix the same by order. FERC stated that the UPSA is "an agreement which 'supplements or supersedes' the coordination arrangements among the MSU utilities and . . . is a contract affecting rates under the 1982 System Agreement (R.167a).[10]

[9] One of the major aspects of the FERC decision was to modify the allocations of such sales among the Middle South operating companies that had been agreed upon by them in the UPSA and to direct corresponding changes in the UPSA and the filing thereof with the FERC.

[10] The District of Columbia panel upheld that analysis, *Mississippi Industries*, 808 F.2d at 1540, and it is not an issue that is the subject of reconsideration on the panel's remand to FERC.

3. The decisions upon which the Mississippi Court purports to rely do not support its position.

The Mississippi Court insists in another part of its opinion (R-21a) that the Mississippi PSC "had the authority, indeed, the duty, to inquire into the prudency" of MP&L's payments to MSE by reason of the rationale of this Court's decision in *Western Distributing Co. v. PSC of Kansas*, 285 U.S. 119 (1932)—a decision which antedated the enactment of the Federal Power Act by more than three years. In that context, the Mississippi Court stated (R-21a):

> We do not read *Nantahala* to the contrary, although it cited with approval several cases involving purchases by closely related entities.

Such a statement is virtually inexplicable.

Nantahala explicitly rests on the "filed rate" doctrine which this Court noted had its genesis for purposes of the Federal Power Act in *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-2 (1951). As summarized in *Nantahala* by this Court, *Montana-Dakota* involved two electric utilities with interlocking directors and joint corporate officers, each of which utilities received some of the other's power at rates that the FPC had determined were reasonable. After separation of the management of the two companies, one brought suit against the other claiming that the rates which it had paid to, and the rates which it had received from, the other were fraudulent and unlawful by reason of the previous interlocking arrangements.

This Court dismissed that claim in *Montana-Dakota*, stating in a portion quoted in *Nantahala* (106 S.Ct., at 2355):

> We hold that the right to a reasonable rate is the right to the rate which the Commission files or fixes, and that, except for review of the Commission's orders, the court can assume no right to a different one on the ground that, in its opinion, it is the only or the more reasonable one.

As the Court pointed out in *Nantahala*, the existence of the interlocking management of the two utilities and the resulting allegations of fraud were irrelevant, again quoting *Montana-Dakota:*

> Perhaps, in the absence of the Commission's approval, such relationship would be sufficient to raise the presumption [of fraud] under state law, but it cannot do so where the federal supervising authority has expressly approved the arrangement.
> *Ibid.*

Moreover, it pointed out that the filed rate doctrine is not a rule of administrative law, but a matter of enforcing the Supremacy Clause.

We submit that the holding in *Western* has been clearly overtaken and replaced by the enactment of the Federal Power Act, the development of the "filed rate" doctrine implementing that Act and the explicit holdings of this Court in *Nantahala* and *Montana-Dakota*.

Similarly, the Mississippi Court's purported reliance upon the portion of the decision in *Appeal of Sinclair Machine Products, Inc.*, 498 A.2d 696, 704 (N.H. 1985), quoted by the Mississippi Court (R.17a), is wholly mistaken.

In that quoted material, the New Hampshire Court explicitly recognized that state regulation of retail electric rates is preempted with respect to matters actually determined by FERC, whether expressly or impliedly. In this case, FERC *expressly* determined the appropriate allocation of Grand Gulf costs among the Middle South companies, including MP&L, and expressly rejected other allocations—including the allocation that MP&L and its affiliates had agreed upon among themselves.

Moreover, *Sinclair* also recognized that, even where matters are not expressly or implicitly resolved by FERC, state regulation is preempted where such state regulation would contradict or undermine FERC determinations or impose inconsistent obligations on the utility companies involved.

On both counts, the Mississippi Court's holding against federal preemption necessarily fails.

The FERC orders obligate MP&L to pay MSE approximately $25 million a month. The record in this proceeding makes it clear that MP&L cannot make such payments to MSE unless MP&L is permitted to charge rates to its customers which make present and/or future provisions for MP&L's obligations to MSE. Specifically, MP&L will be unable to carry out its obligation to make payments to MSE pursuant to the FERC order if its costs of wholesale power are trapped in violation of *Nantahala*.

The Mississippi Court also purports (R-19a) to rely upon the holding of the Fifth Circuit in *New Orleans Public Service Inc.* ("NOPSI") *v. City of New Orleans*, 798 F.2d 858, 862 (5th Cir., 1986) and the application by that court of the abstention doctrine of *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943). But, the Mississippi Court wholly ignores the fact that the last sentence of the material from NOPSI which it quoted stated:

> Nor would federal abstention foreclose the United States Supreme Court from entertaining NOPSI's preemption claim should it wind its way up through the state courts, as is demonstrated by the path of the recent *Nantahala* case.

That is precisely the situation here where, after almost three years of proceedings before the MPSC and Mississippi courts, MP&L's preemption claim has finally "wound its way" through the state commission and courts to this Court by means of MP&L's appeal. It is also worth underscoring that the *Burford* abstention doctrine is addressed to the lower federal courts, on the express premise that:

> . . . if the state procedure is followed from the Commission to the State Supreme Court, ultimate review of the federal questions is fully preserved here. *Burford*, at 334.

Conclusion

The Federal Power Act expressly preempts state action inconsistent with rates filed pursuant to FERC determinations; this Court has so held recently in *Nantahala* as well as in the past. The insistence of state ratemaking bodies and appellate courts on subordinating national interests to parochial concerns has been made abundantly clear; there can be no doubt as to what the issues are or where responsibility lies for the present unwholesome state of affairs. Only this Court can put an end to this dispute.

Moreover, in light of the urgent need for resolution and the clear applicability of *Nantahala*, summary reversal would be appropriate.

Respectfully submitted,

JAMES B. LIBERMAN*
Berlack, Israels & Liberman
1155 Avenue of the Americas
New York, NY 10036
(212) 704-0100
Attorneys for Edison Electric Institute

Of Counsel:
ROBERT L. BAUM
Senior Vice President
and General Counsel
Edison Electric Institute
1111 19th Street, N.W.
Washington, D.C. 20036
(202) 778-6500

August 10, 1987

* Counsel of record.

AMICUS CURIAE

BRIEF

No. 86-1970 (6)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN,
Attorney General of Mississippi, and
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF OF THE ARKANSAS PUBLIC SERVICE COMMISSION, MISSOURI PUBLIC SERVICE COMMISSION AND STATE OF ARKANSAS AS AMICI CURIAE

WALLACE L. DUNCAN
JAMES D. PEMBROKE
J. CATHY LICHTENBERG
DUNCAN, WEINBERG, MILLER
& PEMBROKE, P.C.
1615 M Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 467-6370

Attorneys for the Arkansas Public Service Commission

WILLIAM C. HARRELSON
General Counsel
PAUL H. GARDNER
Deputy General Counsel
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102
(314) 751-2481

Attorneys for the Missouri Public Service Commission

STEVE CLARK
Attorney General
MARY B. STALLCUP
Deputy Attorney General
Justice Building
Little Rock, Arkansas 72201
(501) 371-1967

Attorneys for the State of Arkansas

August 10, 1987

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

16 1/2

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Table of Authorities Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN,
Attorney General of Mississippi, and
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF OF THE ARKANSAS PUBLIC SERVICE COMMISSION, MISSOURI PUBLIC SERVICE COMMISSION AND STATE OF ARKANSAS AS AMICI CURIAE

INTEREST OF THE ARKANSAS PUBLIC SERVICE COMMISSION, MISSOURI PUBLIC SERVICE COMMISSION, AND STATE OF ARKANSAS

The Arkansas Public Service Commission, Missouri Public Service Commission, and State of Arkansas (jointly "Arkansas-Missouri Parties") are vitally concerned that state regulatory commissions retain the ability to perform their statutorily-mandated obliga-

tions such that electric utilities are completely regulated. Those opposing the decision below propose remedies which would emasculate state regulatory authority and leave a substantial gap in the regulation of electric utility companies.

Moreover, Mississippi Power & Light Company ("MP&L"), in its Jurisdictional Statement, fails to address the threshold issue in this case: Whether the Federal Energy Regulatory Commission ("FERC") has jurisdiction over generating facilities such that it may reallocate electric power from a generating facility among subsidiaries of a holding company. If the FERC lacks such jurisdiction, there is no preemption issue to be considered in this case. This jurisdictional issue has been raised by the Arkansas-Missouri Parties in their Petition for a Writ of Certiorari in *Arkansas Public Service Commission et al., v. Federal Energy Regulatory Commission, petition for cert. filed*, 55 U.S.L.W. 3608 (U.S. Feb. 20, 1987)(No. 86-1380).

SUMMARY OF ARGUMENT

Prior to determining the instant case, this Court must decide the threshold issue: Whether the FERC has jurisdiction to regulate generating facilities by reallocating the costs of or output from a generating plant. The Federal Power Act specifically states that the FERC cannot do so. *See* 16 U.S.C. § 824(b)(1)(1982). If the FERC lacks such authority, no Supremacy Clause issue can arise in this case, and utilities may be fully regulated by the states.

Any decision which grants the FERC exclusive jurisdiction in this area will result in a substantial regulatory gap and will undermine the purposes of the Public Utility Holding Company Act ("PUHCA"),

which is intended to allow continued effective state regulation of subsidiaries of holding companies.

ARGUMENT

The Threshold Question: Can the FERC Regulate Generating Facilities?

The preemption issue herein arises in the context of a decision by the FERC reallocating the costs of the Grand Gulf Unit No. 1 nuclear power plant ("Grand Gulf") among four Middle South Utilities ("MSU") operating companies.[1] In *Middle South Energy, Inc. and Middle South Services, Inc.*,[2] the FERC considered a unit power sales agreement ("UPSA") among the four MSU operating companies, which contractually divided the output of Grand Gulf as follows:

Grand Gulf

	Percentage	Megawatts[3]
AP&L:	0%	0
LP&L:	38.57%	433.9
MP&L:	31.63%	355.8
NOPSI:	29.80%	335.3

[1] Those operating companies are Arkansas Power & Light Company ("AP&L"), Louisiana Power & Light Company ("LP&L"), MP&L and New Orleans Public Service, Inc. ("NOPSI").

[2] Middle South Energy, Inc. and Middle South Services, Inc., 31 FERC (CCH) ¶ 61,305, *aff'd on reh'g*, 32 FERC (CCH) ¶ 61,425 (1985), *aff'd sub nom.* Mississippi Industries v. FERC, 808 F.2d 1525 (D.C. Cir.), *reh'g en banc granted and vacated in part*, 814 F.2d 773, *reh'g en banc denied, reh'g granted and vacated in part*, ___ F.2d ___ (D.C. Cir. June 24, 1987), *petitions for cert. filed*, 55 U.S.L.W. 3608, 55 U.S.L.W. 3622 (U.S. Feb. 20, 1987, March 4, 1987)(Nos. 86-1380 & 86-1424).

[3] The term "megawatt" is a unit of measure of electric generating capacity equal to 1,000 kilowatts or 1,000,000 watts.

The FERC modified the contract and reallocated the responsibility to purchase electric capacity and energy from Grand Gulf as follows:

	Grand Gulf Percentage	Megawatts
AP&L:	36%	405
LP&L:	14%	158
MP&L:	33%	371
NOPSI:	17%	191

In other words, the FERC reviewed the cost of and power allocation from a generating facility and reallocated the costs of and power from that facility despite the clear and total absence in the Federal Power Act of a grant of jurisdiction to regulate generating facilities. *See* 16 U.S.C. § 824(b)(1)(1982)[4].

The FERC simply has no jurisdiction to reallocate the costs or output of a generating plant. Because no jurisdiction exists, FERC cannot preempt the right

[4] The Federal Power Act provides:

> The Commission . . . shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy. . . .

16 U.S.C. § 824(b)(1)(1982). In the *Middle South* proceeding, neither the court below nor the FERC pointed to any part of the Federal Power Act which would have authorized its jurisdiction over generation in this instance. Rather, the court below asserted that "FERC may lawfully assert jurisdiction over matters pertaining to generation where it is found that generation facilities are used as facilities for interstate wholesale sales." Jurisdictional Statement, Appendix at 42a-43a. This purported "limitation" is meaningless in an industry in which virtually every generating facility is a part of an interstate network and the FERC only regulates wholesale sales.

of state commissions to examine the prudence of such plant. Thus, the issue of the existence of FERC jurisdiction must be resolved before this Court examines whether the FERC jurisdiction preempts the state commission from acting.

The Decision Below: Allowable State Prudence Review

The decision below allowed the Mississippi Public Service Commission ("MPSC") to determine various questions of prudence regarding Grand Gulf, including: (1) whether the decision to construct Grand Gulf was prudent; (2) whether the decision to continue Grand Gulf construction was prudent; (3) whether the costs for construction of Grand Gulf were prudently incurred; (4) whether the construction, completion and operation of Grand Gulf was prudent in light of available alternatives for electric power supply. *See State of Mississippi v. Mississippi Public Service Commission*, Jurisdictional Statement, Appendix at 17a. Contrary to allegations by MP&L, FERC and the United States, the Court below did not direct the MPSC to relitigate the formula derived by the FERC. Rather, the MPSC could determine the prudence of the total cost of Grand Gulf[5] and, if the MPSC determined any portion of that total amount to be imprudently incurred, it could disallow the imprudently incurred cost and apply the FERC formula to the reduced total Grand Gulf cost.

[5] In determining the prudence of the cost of a unit built by a nonjurisdictional generating subsidiary, a state regulatory agency could investigate the prudence of the generating subsidiary and impute any imprudence to jurisdictional sister companies within the holding company structure. *See* Commonwealth Electric Co. v. Department of Public Utilities, 397 Mass. 361, 491 N.E.2d 1035 (1985), *cert. denied*, 107 S. Ct. 1971 (1987).

MP&L, FERC and the United States attempt to portray the state regulatory commissions as parochial entities seeking to transfer the costs of expensive power plants onto consumers of other states. These contentions do not properly reflect the facts. This review of the prudence of construction, continuation of construction, and cost of Grand Gulf would not result in a reallocation of costs among the consumers of other states. Rather, it would result in a reallocation of costs between stockholder and ratepayer. In any unregulated industry, stockholders, as a practical matter, must pay for management imprudence. Proper regulation of the electric utility industry should also require stockholders to pay for management imprudence. The prudence investigation discussed by the Court below would lead to enhanced management responsibility, an appropriate goal of effective regulation.[6]

Utilities naturally seek to minimize regulation of their activities and to maximize their shareholder profit. Therefore, it is to their advantage to place any prudence review in a favorable forum which is unlikely to find imprudence of construction or continuation of a power plant. Although imprudence has been raised before the FERC on numerous occasions,[7]

[6] Decisions of the state regulatory commissions are governed by legal and constitutional constraints. To the extent that any state regulatory commission was overzealous in its allocation of costs between stockholder and consumer, it would be subject to review and reversal in the courts for any action which is arbitrary and capricious or unsupported by substantial evidence.

[7] *See, e.g.*, New England Power Co., 31 FERC (CCH) ¶ 61,147 (1985); Connecticut Light and Power Co., 5 FERC (CCH) ¶ 63,004 at 65,071 (1978), *aff'd* 13 FERC (CCH) ¶ 61,155 (1980);

it has been found only once, notably after a prior state regulatory commission finding of imprudence. *See Union Electric Co.*, 40 FERC (CCH) ¶ 61,046 (1987). Imprudence has been found at the state level on numerous occasions. *See Kansas Gas and Electric Co. v. State Corp. Comm'n*, 239 Kan. 483, 720 P.2d 1063 (1986), *prob. juris. noted*, 107 S. Ct. 1281 (1987); *Commonwealth Electric Co. v. Department of Public Utilities*, 397 Mass. 361, 491 N.E.2d 1035 (1985), *cert. denied*, 107 S. Ct. 1971 (1987); *Re Long Island Lighting Co.*, 71 PUR 4th 262 (1985). MP&L here seeks a decision that the FERC is the only forum which may examine prudence involving a generating subsidiary of a regulated company.[8] Such decision would be contrary to the traditional prudence review of generating facilities by state regulatory commissions. For example, if a generating facility is owned by a single utility or jointly owned by a number of utilities, it is unquestionably subject to state, rather than federal, prudence regulation. *See* Ark. Stat. Ann. § 73-276 through 73-276.18 (1979). Moreover, any decision that generating facilities may be regulated only by the FERC and never by the states, where those generating facilities are owned by a subsidiary company, would encourage utility management to create or dis-

Southern California Edison Co., 59 FPC 2167, 2176 (1977), *aff'd* 2 FERC (CCH) ¶ 61,018 (1978).

[8] Contrary to the contentions of MP&L, FERC and the United States (*see* Jurisdictional Statement at 7-8, n.5, Amici Brief at 14, n.6), neither the FERC nor the Presiding Administrative Law Judge at the FERC made any determination of the prudence of Grand Gulf. At the cited page, the Presiding Administrative Law Judge stated that MSU determined the prudence of Grand Gulf. *See* 26 FERC (CCH) at 65,112-13. The prudence of Grand Gulf was not an issue litigated or decided at the FERC.

solve subsidiary companies so as to subject the plant to the jurisdiction of the regulatory body which management perceives most favorable, be it the state or federal commission.

Further, recognizing only FERC, and not state, regulation of generating facilities will result in a regulatory gap. The FERC has generally declined to determine the prudence of purchase of power except in the limited circumstance where a utility includes an allegedly imprudent purchase of power as an expense item in a wholesale rate proceeding.[9]

The FERC has never examined the prudence of construction or continuation of construction of a generating facility outside the context of a general wholesale rate filing. Nor could it do so because of the generating facility exemption in the Federal Power Act. *See* 16 U.S.C. § 824(b)(1) (1982).

If the states are precluded from regulating prudence of purchase in any wholesale power situation, the utilities will effectively escape regulation by forming generating subsidiaries.

The logical solution to this regulatory dilemma is a strict and appropriate interpretation of the FERC's

[9] *See* Monongahela Power Co., 39 FERC (CCH) ¶ 61,350 at 62,095 (1987); Southern Company Services, Inc., 28 FERC (CCH) ¶ 61,349 (1984); Pacific Power & Light Co., 27 FERC (CCH) ¶ 61,080 at 61,148 (1984); Pennsylvania Power & Light Co., 23 FERC (CCH) ¶ 61,325 at 61,716 (1983). The FERC has suggested that only the FERC could regulate prudence of purchase in a power pooling or holding company situation. *See* AEP Service Corp., 32 FERC (CCH) ¶ 61,363 (1985); AEP Generating Co., 29 FERC (CCH) ¶ 61,246 (1984). *See also* Nixon and Johnston, *Nantahala Affirms Narragansett - Whither Pike County?* 8 Energy L. J. 1, 7-12 (1987).

jurisdictional limitations. If the FERC lacks jurisdiction over generating facilities—as is stated in the Federal Power Act—it cannot reallocate power from a generating plant to the subsidiaries of a holding company. States are then free to conduct necessary prudence reviews without constitutional constraints resulting from the Supremacy Clause.

State Jurisdiction Over Holding Company Subsidiaries.

In their Amici Brief, the FERC and the United States suggest that in a holding company situation, there is no role for a state regulatory commission. *See* Amici Brief at 14. This proposition directly undermines the PUHCA, 15 U.S.C. §§ 79a, 79b, 79h, 79k (1982). PUHCA was specifically designed to allow continued effective state regulation of holding company subsidiaries. In order to allow the holding company to continue in existence, the Security and Exchange Commission must find:

> The continued combination of such systems under the control of such holding company is not so large . . . as to impair the advantages of localized management, efficient operation, or the *effectiveness of regulation*.

15 U.S.C. § 79k(b)(1) (emphasis supplied). One of the purposes of the PUHCA was to protect the national public interest and the interest of consumers of electricity who "are or may be adversely affected—"

> when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies. . . .

15 U.S.C. § 79a(b). In other words, a state regulatory commission must be able to regulate holding company subsidiaries effectively. Allowing holding company subsidiaries to escape state regulation by purchasing power from an affiliate is antithetical to the purposes of PUHCA.

CONCLUSION

This Court need not reach the preemption issue because the FERC lacks jurisdiction over generating facilities and, therefore, the state commissions have exclusive jurisdiction over the prudence of Grand Gulf. The FERC may not assert a greater jurisdiction over Grand Gulf because it is owned by a holding company subsidiary without undermining the principles of PUHCA, which seeks to maximize effective state regulation of holding company subsidiaries.

Respectfully submitted,

WALLACE L. DUNCAN
JAMES D. PEMBROKE
J. CATHY LICHTENBERG
DUNCAN, WEINBERG, MILLER
& PEMBROKE, P.C.
1615 M Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 467-6370

Attorneys for the Arkansas Public Service Commission

WILLIAM C. HARRELSON
General Counsel
PAUL H. GARDNER
Deputy General Counsel
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102
(314) 751-2481

Attorneys for the Missouri Public Service Commission

STEVE CLARK
Attorney General
MARY B. STALLCUP
Deputy Attorney General
Justice Building
Little Rock, Arkansas 72201
(501) 371-1967

Attorneys for the State of Arkansas

AMICUS CURIAE

BRIEF

9

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN,
Attorney General of Mississippi and
MISSISSIPPI LEGAL SERVICES COALITION,

On Appeal from the Supreme Court of Mississippi

BRIEF FOR THE COUNCIL OF THE CITY OF NEW ORLEANS AS AMICUS CURIAE

OKLA JONES, II
City Attorney
BRUCE E. NACCARI
Assistant City Attorney
BEVERLY ZERVIGON
Deputy Director
Council Utility Regulatory
Office
1300 Perdido Street
New Orleans, Louisiana 70112
(504) 586-4651

WALTER J. WILKERSON
Suite 2720, Poydras Center
650 Poydras Street
New Orleans, Louisiana 70130
(504) 522-4572

CLINTON A. VINCE*
BERNHARDT K. WRUBLE
NANCY A. WODKA
VERNER, LIIPFERT, BERNHARD,
McPHERSON AND HAND, Chartered
1660 L Street, N.W.
Suite 1000
Washington, D.C. 20036
(202) 775-1000

KENNETH M. CARTER
SIDNEY H. CATES
CARTER & CATES
Suite 1850, Energy Center
New Orleans, Louisiana 70163
(504) 569-2005

Counsel of Record

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

23 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Table of Authorities Continued

Table of Authorities Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN, Attorney General, and
THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees,

BRIEF FOR THE COUNCIL OF THE CITY OF NEW ORLEANS AS AMICUS CURIAE

STATEMENT OF INTEREST

This brief *amicus curiae* is presented on behalf of the Council of the City of New Orleans (the "Council") by, *inter alia*, its authorized legal officer. The Council has, under Louisiana law, plenary authority to regulate the retail electric rates charged by New Orleans Public Service, Inc. ("NOPSI") to ratepayers in Louisiana. NOPSI, like Mississippi Power & Light Company ("MP&L"), appellant here, is a wholly-owned subsidiary of Middle South Utilities, Inc. ("MSU") and is a purchaser of electric power from the Grand Gulf 1 nuclear plant owned by System

Energy Resources, Inc. ("SERI"), another MSU subsidiary.

Since 1985, the Council has been involved in retail ratemaking proceedings related to NOPSI's request for an increase in rates to cover its share of the Grand Gulf costs, and in two federal court proceedings by which NOPSI has attempted to prevent the Council from exercising its retail ratemaking functions, including a review of NOPSI's prudence in relation to the retail rate aspects of the Grand Gulf purchases.[1] The Council has two important concerns.

[1] In the first federal court proceeding, *New Orleans Public Service, Inc. v. City of New Orleans*, 782 F.2d 1236, *withdrawn in part*, 798 F.2d 858 (5th Cir. 1986), *cert. denied*, 107 S. Ct. 1910 (1987) (hereinafter, "*NOPSI I*"), NOPSI sought an injunction ordering the Council to pass through to ratepayers, immediately and without exercising traditional regulatory functions, increases that threatened a "severe rate shock effect" on New Orleans. *NOPSI I*, Civ. Act. No. 85-3398, slip op. at 5 (E.D. La., Sept. 16, 1985). That action was dismissed by the district court on the basis of the abstention doctrine, ultimately affirmed by the Court of Appeals in *NOPSI I*. This Court denied review on April 20, 1987. The retail rate case was settled by an order involving a phase-in plan to moderate rate shock as well as partial cost absorption by NOPSI. *See* Council Res. No. R-86-112 (Mar. 20, 1986.)

In October, 1985, the Council instituted an investigation into the prudence of NOPSI's actions with regard to Grand Gulf 1 as part of the retail ratemaking proceeding. NOPSI initiated a second federal court proceeding to enjoin the investigation. That case was dismissed in December 1986 on the basis, *inter alia*, of the abstention doctrine and lack of ripeness, and is presently before the Fifth Circuit. *New Orleans Public Service, Inc. v. City New Orleans*, Civ. Act. No. 85-5273 (E.D. La. dismissed Dec. 19, 1986), *appeal docketed*, No. 87-3049 (5th Cir., Jan. 23, 1987) (hereinafter, "*NOPSI II*"). The aforesaid settlement permitted the Council to continue its prudence inquiry.

First, the arguments made by, and grounds for review proposed by, appellant are so broad that they might adversely affect the Council's position in discharging its retail regulatory responsibilities, despite significant factual differences between the New Orleans situation and that in Mississippi.[2] Second, there are critical defects and misconceptions in the substance of appellant's arguments that require response.

Two major misconceptions fostered by MP&L's jurisdictional statement are: (1) that the Federal Energy Regulatory Commission ("FERC") conducted a prudence review when it allocated the Grand Gulf costs among the MSU companies; and (2) that the Mississippi proceedings are ripe for this Court's review as a "final" decision of the highest Mississippi court.

The FERC did not consider prudence in its determination of the Grand Gulf wholesale rates. Rather, its own administrative law judge expressly rejected attempts to inject considerations of prudence, espe-

[2] In New Orleans, the Council put into effect increased retail rates substantially reflecting the costs of Grand Gulf 1 under the phase-in plan contained in the March 1986 settlement. The prudence inquiry was, pursuant to the settlement, allowed to take its own course. Therefore, the prudence inquiry did not result in either a denial of a rate increase or a refund order; and no monetary rate penalty (if any) could be imposed until the evidence on imprudence were heard and a decision rendered. Moreover, the Council specifically recognized the FERC's wholesale rate allocation and stated that the Council would not seek to invalidate any interstate contracts or to have NOPSI pay a rate other than as prescribed by the FERC. (Council Res. No. R-85-636, Oct. 17, 1985.) The prudence inquiry itself has focused on whether NOPSI's management acted prudently in respect to matters and alternatives *not* foreclosed by either the FERC's allocation or interstate contracts approved by the FERC.

cially at the retail level, into the case. The former FERC Acting Chairman testified in Congress that no prudence inquiry had been undertaken. State regulatory bodies have not been preempted from conducting prudence inquiries that bear on the establishment of retail rates for Grand Gulf.

In this case, however, the Court should not reach the preemption issue in order to dispose of this appeal. The Mississippi Public Service Commission ("MPSC") should be given the opportunity to conduct a prudence inquiry that accords with both its state law and federal constitutional obligations, and the result thereof should be reviewed by the state supreme court. There should be a "final" decision emanating from Mississippi before this Court undertakes review in a delicate area of shared state and federal jurisdiction. This preferred course of action can be accomplished here while the *status quo* is preserved.

Allowing the case to go forward at the state level would put it in the same posture for review as *Nantahala Power & Light Co. v. Thornburg*, 106 S. Ct. 2349 (1986). There, the initial decision of the state utility commission was reversed by the state supreme court. The state commission had the opportunity to act with finality on the merits, with review by the state court. No substantive decision on the issue of prudence has been rendered here. No determination can be made on the present record whether the MPSC will take any action preempted by federal law or whether the Mississippi Supreme Court will decide the case wrongly once an active prudence decision is before it.

The Council respectfully suggests that the Court either dismiss or postpone hearing the appeal, or that

it affirm the decision below, while preserving the present stay pending the state proceedings—so that this Court's jurisdiction to hear the case in final form will be preserved.

ARGUMENT

I. AS THE FERC DID NOT CONSIDER ISSUES OF PRUDENCE IN ALLOCATING THE GRAND GULF COSTS ON EITHER THE WHOLESALE OR RETAIL LEVEL, STATE COMMISSION REVIEW OF THE UTILITY'S PRUDENCE WAS NOT PREEMPTED

MP&L's appeal asserts that state review of MP&L's prudence[3] was preempted by the FERC's allocation

---

[3] A prudence inquiry is a traditional ratemaking function, based on the established principle that costs may be passed on to ratepayers only to the extent they are prudently incurred. *Missouri ex rel. Southwestern Bell Tel. Co. v. Public Service Commission*, 262 U.S. 276 (1923). This reflects the policy that bad business judgment is not the risk of the ratepayers, but the risk of the owners. As articulated in a recent study:

> The concept of a prudent investment in public utility law is a regulatory oversight standard that attempts to serve as a legal basis for judging whether utilities meet their public interest obligations. . . .
>
> * * *
>
> The concept of prudence provides commissions with a principle that does not necessarily require an 'all or nothing' decision in favor of some side, but can allow some sharing of the risks between investors and the ratepayers. The prudent investment test is a tool that regulators are using to provide an answer to the question of who should bear which risks and associated costs.

Burns, Poling, Whitman & Kelly, *The Prudent Investment Test in the 1980s* (The National Regulatory Research Institute, 1985) at iv, vi.

of Grand Gulf 1 costs among the MSU operating subsidiaries. This is false. No considerations of management prudence were involved in FERC's determination of an appropriate allocation of the Grand Gulf costs among the MSU operating companies.

At the outset of the Grand Gulf cost allocation hearings, the Presiding Judge and the parties defined the issues that would be tried. Counsel for SERI (Mr. Merriman) repeatedly tried to draw Presiding Judge Liebman into making indirect or implied rulings on prudence, but was rejected:

> MR. MERRIMAN:
>
> * * *
>
> Now, Middle South Energy is exclusively subject to the jurisdiction of the FERC. It is a 100 percent wholesaler. We don't want somebody later someplace to say that therefore the costs involved in that construction were somehow unjust and unreasonable because you did something wrong.
>
> PRESIDING JUDGE: Okay.
>
> But I can't preclude parties here from somewhere else raising anything they want to raise. And the only thing that I'm concerned about is what matters I should decide. And as far as I can see I don't have to decide the issue of the prudence of the construction—of the decision to construct the Grand Gulf project.

Middle South Energy, Inc., Docket No. ER82-616-000, Transcript of Proceedings, March 14, 1983, at 235-36.

The Presiding Judge indicated that he would not rule on any issue involving the prudence of the individual MSU operating companies:

> MR. O'SULLIVAN: I just wanted to make sure that there was no confusion between the prudence inquiries that I understand you ruled this morning *the states were entitled to make.*
>
> That is, *the prudence of the affiliates* under the jurisdiction of the states making a purchase of Grand Gulf power for purposes of retail resale, and that that issue is not stipulated, the buyers is not stipulated to.
>
> PRESIDING JUDGE: *I'm not getting into that* I don't think in this case.
>
> MR. MERRIMAN: He's not saying one way or the other what the jurisdiction of the state commissions are.
>
> PRESIDING JUDGE: *I'm not getting into that.*

(*Id.* at 228). (Emphasis added.)

At the close of the relevant dialogue, the Presiding Judge said to Mr. Merriman:

> PRESIDING JUDGE: *I don't think you can put me in a position or this Commission in a position of deciding a prudency issue on the allocation issue in such a way that no one can possibly raise this in the State Court.* I think that's the problem you have. I may be wrong.

> I don't intend to get into state jurisdiction, but I do intend to get into what a fair and just and reasonable and non-discriminatory rate schedule and agreement is.
>
> MR. EASTLAND: *Wholesale* level.
>
> PRESIDING JUDGE: At the *wholesale* level.

(*Id.* at 248). (Emphasis added.) Thereafter, the Presiding Judge listed fourteen issues to be the subject of the case, but did not include any reference to prudence. (*Id.* at 248-51).[4] No issue of prudence was litigated *either* at the wholesale, interstate level (which would have been within FERC jurisdiction) or at the retail, state level (which would not.)[5]

The FERC did not purport to preempt the functions of the retail regulatory bodies; did not address the

---

[4] Failing to mention the foregoing exchanges, appellant instead quotes (at p. 7, n.5) a passage from Judge Liebman's initial decision in which he used the word "prudent"—in a different context. Judge Liebman was not determining whether the companies' actions were prudent, but rather was setting forth his view as to how the reason for building the plant changed over time. 26 FERC ¶ 63,044 (1984) at p. 63,112. Thus, he used the word "prudent" to describe a *subjective* belief of the Middle South executives, which is *not* the legal test of prudence in utility law. Should there be any doubt, Judge Liebman's statements can be contrasted with those made in his recent decision in *Kansas Gas and Electric Co.*, 39 FERC ¶ 63,013 (1987) at pp. 65,058-69, in which prudence was an issue.

[5] Nor was any issue of prudence tried in the case governing the allocation of the costs of all generating facilities on the MSU system, *Middle South Energy, Inc.*, 30 FERC ¶ 63,030 (1985). Although never formally consolidated with the Grand Gulf allocation proceeding, the Commission's Opinion Nos. 234 and 234-A covered both *Middle South* dockets.

manner, timing, or extent of recovery by the operating companies of Grand Gulf costs; did not mandate immediate or complete pass through of such costs in retail rates; and did not bar retail regulators from investigating questions of prudence of the operating companies.

Rather, the FERC acknowledged the traditional role of the states in retail ratemaking regulation:

> [W]e concurred in [Judge Head's] discussion of the need to balance Federal and states interests in exercising our jurisdiction. Furthermore, we think our opinion, taken as a whole, as well as Judge Head's discussion, which we adopted, clearly recognize the role of the states in regulating the retail electric rates and the need to balance overlapping state and Federal electric rate jurisdiction.

Middle South Energy, Inc., 31 FERC ¶ 61,305 (1985) at p. 61,951. The FERC subsequently concluded:

> The basic nature of regulatory control retained by the states under previous System agreements remains unchanged. What our decision attempts to do is amend the filed agreements to achieve a non-discriminatory sharing of excess capacity cost imbalances on the integrated System, consistent with the goal of the System Agreement, and to do so with as little intrusion on the States as possible.

Id. at p. 61,952.[6]

---

[6] FERC, in a self-serving twist of the facts, asserts in its

The then-Acting Chairman of the FERC confirmed in Congressional testimony that the FERC did not determine prudence issues in the Grand Gulf cost allocation hearings:

> The Commission *did not determine the prudence* of the purchase of power by the Middle South utilities from the Grand Gulf Nuclear Generating Station in Opinion Nos. 234 and 234-A.[7]

Allowing the states the opportunity to deal with the retail implications of wholesale rate increases re-

---

amicus brief that none of the parties argued before it that the costs of Grand Gulf 1 were not prudently incurred. *See* Brief for the United States at p. 14 n.6. The Commission ignores the admonitions of its own administrative law judge, cited above, that he was "not getting into that [*i.e.*, a prudence inquiry] . . . in this case." The FERC also misportrays, as does MP&L (*see* note 4, *supra*), Judge Liebman's reference to the company's executives' subjective belief that their actions were "prudent" as a "finding" that the construction of Grand Gulf 1 was prudent. No such finding was made by Judge Liebman; rather, he declined to determine such issues, and the Commission, in reviewing the Judge's decision, did not address prudence. Had the FERC done so, the parties could have appealed that aspect of the decision to the D.C. Circuit. Instead, the FERC failed to act in an area in which its jurisdiction is not exclusive, and its attorneys now attempt to portray the FERC's inaction as an exercise of exclusive authority. It is significant that no one has conducted a prudence review of the MSU companies' management of the Grand Gulf construction at the wholesale or retail level.

[7] Submission to the Subcommittee on Energy Submission to the Subcommittee on Energy Conservation and Power of the House of Representatives Committee on Energy and Commerce, Hearing on Prudence Reviews (March 14, 1986). (Emphasis added).

affirms the "bright line" that exists between federal regulation of sales "at wholesale to local distributing companies" and state regulation of the sale of power at "local retail rates to ultimate consumers." *See Federal Power Commission v. Southern California Edison Co.*, 376 U.S. 205, 214 (1964); *Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 379-80 (1983). As stated by the Fifth Circuit in *NOPSI I*:

> The existence of this 'bright line' colors the way we view a preemption claim involving the Federal Power Act. NOPSI has attempted to depict the situation before us as one in which the Council is stepping into the realm of *wholesale* rate making, a field under the exclusive jurisdiction of FERC. NOPSI focuses on the disruption of a *federal* scheme. Yet federal court intervention here may constitute a disruption of a *state* regulatory scheme, for *retail* rate making is clearly a field left to the jurisdiction of the states.

798 F.2d at 860 (emphasis added).

The *Nantahala* case, relied upon by MP&L, does not alter the authority of states to conduct the type of prudence investigation at issue here, as an element of retail ratemaking. Moreover, no issue of imprudent management was presented in *Nantahala*. In that case, the FERC had adopted a formula for allocation of costs between utilities located in different states. North Carolina, believing that its ratepayers should receive a more favorable allocation, simply substituted its own formula (as the basis for retail rates) for the FERC's. With no competing considerations present,

this Court held that the "filed rate doctrine" prevented the adoption of a contradictory formula and required the state to pass through the wholesale costs in order to avoid their "trapping". 106 S. Ct. at 2359. The Court, however, made it clear that other, traditional retail ratemaking actions (there, the recognition of offsetting costs) could properly be taken into consideration in establishing retail rates. *Id.* at 2357-58. *See also NOPSI I*, 798 F.2d at 860-61.

Nantahala does not purport to exhaust the remedies or approaches that may be taken in a retail rate setting under different sets of facts. If, for example, management has been derelict in pursuing opportunities to hedge against or otherwise alleviate the risks posed by large, speculative projects, it does not follow that the ratepayer must bear the full cost in all events. As the FERC did not consider such issues of management prudence in the Grand Gulf cost allocation proceeding, state regulatory bodies have not been preempted from examining the issue in the establishment of retail rates for Grand Gulf.

II. SINCE THE MISSISSIPPI COURT HAS NOT RENDERED A FINAL DECISION WITHIN THE MEANING OF 28 U.S.C. § 1257(2), THIS APPEAL IS NOT RIPE.

Final action has not been taken here by the State of Mississippi. Review by this Court of a state court decision is limited to "[f]inal judgments or decrees rendered by the highest court of a State in which a decision could be had. . . ." 28 U.S.C. § 1257(2). The state court decision "must be subject to no further review or correction in any other state tribunal; it must also be final as an effective determination of the litigation and not of merely interlocutory or in-

termediate steps therein. It must be the final word of a final court." *Market Street Ry. Co. v. Railroad Commission*, 324 U.S. 548, 551 (1945).[8] No such finality exists here. The Mississippi Supreme Court has remanded the case for further consideration by the MPSC. The MPSC is the only body authorized to frame and conduct a retail prudence hearing at the retail level under Mississippi law, and it has not yet particularized its investigation or begun its review. There is no record on which this Court may determine whether the State will actually take any action preempted by the FERC's allocation or otherwise by federal law.[9] The only pressing issue—the impact of

---

[8] In the context of state court review of an administrative agency decision, the agency order must be the final adjudication in a completed administrative process, and must establish legal rights and relationships to which liabilities or sanctions may attach. Stern, Gressman & Shapiro, *Supreme Court Practice* 135 (6th ed. 1986), citing *Republic Natural Gas Co. v. Oklahoma*, 334 U.S. 62, 69-72 (1948); *Laclede Gas Light Co. v. Public Service Commission*, 304 U.S. 398 (1938). Thus, in *Laclede*, where the Missouri Supreme Court upon review of a Missouri PSC rate order remanded the cause with directions that the commission redetermine certain facts in accordance with the views of the court, the adjudication was not "final." *Id.* at 400.

[9] The opinion of the Mississippi Supreme Court is unclear as to the nature of the proposed prudence inquiry, and uses the word "prudence" in shifting senses and different contexts, including several which vary from normal usage. For example, it refers to the "prudency of their [sister MSU companies'] operation" or the "fairness of their many 'in-house' dealings" (App. 13a); to "a price that is not prudent," (App. 15a); to the 1982 System Agreement as seeming to be imprudent (App. 16a); to the prudence of putting the plant on line (App. 17a); and to the prudency of MP&L's investment in the plant (App. 19a). The court raises issues which it suggests should have been considered

the Mississippi court's original orders curtailing rates and imposing a refund—has been remedied by a stay, and the resulting *status quo* may be preserved pending final state action.

MP&L argues that in light of *Nantahala any* inquiry into its prudence has been preempted by the FERC's actions. *Nantahala* does not purport to deal at all with the proper scope and effect of a prudence inquiry at the state level or appropriate relief in varying factual circumstances. Rather, it recognizes traditional retail functions. Clearly, there are areas into which the MPSC may inquire and act without violating the principles of federal supremacy, but those areas remain undefined on the present record.[10] Until the MPSC completes the proceeding, and the Mississippi Court has the the opportunity to review the administrative decision and determine any federal questions MP&L may raise in the context of such

by the MPSC in approving MP&L's retail rate increases, but nowhere does the court establish clear parameters for the agency's review. On this record, it cannot be presumed that the MPSC will investigate areas preempted by FERC action (if any) or that it will fashion a remedy for any management imprudence it finds that will conflict with federal law.

[10] FERC, in its *amicus* brief, speculates that the MPSC can reach only one of two decisions as a result of its prudence inquiry: either 1) that MSU was imprudent and that its shareholders should bear some of the costs of Grand Gulf, or 2) that MP&L was imprudent and that a portion of its share of the costs should therefore be borne by the ratepayers of its sister companies in other states. The FERC ignores a third, entirely plausible outcome: that MP&L could be found imprudent in not having arranged for alternative uses of its Grand Gulf share (*e.g.*, off-system sales) and that absorption of some of the costs by MP&L's shareholder is therefore appropriate.

proceedings, no finality can be accorded to the State's determinations. "[W]here further proceedings on remand will shed additional light on the record, and thereby remove factual ambiguities that preclude an informed judgment on a constitutional issue, there is a compelling reason for concluding that a final judgment has not yet been rendered." Stern, Gressman & Shapiro, *Supreme Court Practice* 129 (6th ed. 1986), citing *Minnick v. California Department of Corrections*, 452 U.S. 105 (1981).

This was substantially the course followed by the *Nantahala* litigation before it was reviewed by this Court. The North Carolina Supreme Court reversed and remanded a decision of the state utility commission which decision, in effect, overturned the commission's implementation of an interstate allocation decision, but the federal courts declined to interfere in the case.[11] The matter was then decided by the state utility commission and reached the state supreme court for final review. *State ex rel Utilities Commission v. Nantahala Power and Light Co.*,. 313 N.C. 614, 332 S.E.2d 397 (1985). This was the decision reviewed by the Court in *Nantahala*.

Several exceptions to the finality requirement have been recognized by the Court. *See Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 486 (1975). None of these exceptions, which are addressed in the brief of the appellees, is applicable here. Moreover, this Court has confirmed that an expansive construction of the Cox exceptions would "swallow the rule" of finality.

[11] *See Aluminum Company of America v. Utilities Commission of the State of North Carolina*, 713 F.2d 1024, 1026-27 (4th Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984).

Flynt v. Ohio, 451 U.S. 619, 622 (1981). Mississippi should be permitted to develop a factual record on prudence and to articulate a response to MP&L's claims in the context of that record. This is the model contemplated by *Nantahala*. Only in this manner can the Court avoid unnecessary federal intrusion into state affairs, a key underpinning of the final judgment rule. *See North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc.*, 414 U.S. 156, 159 (1973); *Radio Station WOW v. Johnson*, 326 U.S. 120, 123-24 (1945).

III. MP&L CAN BE PROTECTED FROM ALLEGED HARM PENDING COMPLETION OF THE PRUDENCE REVIEW AND ANY ADDITIONAL STATE COURT PROCEEDINGS

The additional action taken by the Mississippi Supreme Court in remanding the case—its rate curtailment and refund order—differs from the action taken by the Council and may require specific treatment by this Court in order to preserve its own jurisdiction ultimately to hear the appeal. There are at least three procedures available to the Court pursuant to which MP&L, and thus this Court's jurisdiction, can be protected pending ultimate review by this Court, and yet which would also avoid premature federal intrusion into the state's affairs.

The Court could note probable jurisdiction of the appeal,[12] maintain its stay in effect, and postpone further consideration until after the MPSC prudence investigation is complete and the state court review of

---

[12] The Court also may issue an order postponing consideration of jurisdiction to a later hearing on the merits. Supreme Court Rule 16.7.

the decision has been rendered, if sought. Alternatively, the Court could issue an order stating that it will defer review of this matter and dismissing the appeal on the condition that the Mississippi Supreme Court take appropriate action to maintain the *status quo* pending completion of the prudence review and any appeals thereof.

The Court also has authority pursuant to the All Writs Act, 28 U.S.C. § 1651, to issue "all writs necessary or appropriate in aid of [its jurisdiction] and agreeable to the usage and principles of law." Thus, even upon dismissal of the appeal or affirmance of the decision below, an order could be entered directing the Mississippi Supreme Court to take action necessary to maintain the *status quo*. *See Ex Parte United States*, 287 U.S. 241 (1932); *see also Ex Parte Republic of Peru*, 318 U.S. 578 (1943); *National Farmers' Organization, Inc. v. Oliver*, 530 F.2d 815 (8th Cir. 1976).

IV. CONCLUSION

For the foregoing reasons, the Council respectfully suggests that the Court defer consideration of the appeal by one of the means recited above or by other appropriate means.

Respectfully submitted,

CLINTON A. VINCE*
BERNHARDT K. WRUBLE
NANCY A. WODKA
VERNER, LIIPFERT, BERNHARD
MCPHERSON AND HAND, Chartered
1660 L Street, N.W.
Suite 1000
Washington, D.C. 20036
(202) 775-1000

OKLA JONES, II
City Attorney
BRUCE E. NACCARI
Assistant City Attorney
BEVERLY ZERVIGON
Deputy Director
Council Utility Regulatory Office
1300 Perdido Street
New Orleans, Louisiana 70112
(504) 586-4651

KENNETH M. CARTER
SIDNEY H. CATES
CARTER & CATES
Suite 1850, Energy Center
New Orleans, Louisiana 70163
(504) 569-2005

WALTER J. WILKERSON
Suite 2720, Poydras Center
650 Poydras Street
New Orleans, Louisiana 70130
(504) 522-4572

*Counsel of Record

August 10, 1987

JOINT APPENDIX

18

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI, ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court
of Mississippi

JOINT APPENDIX

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, DC 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.

Attorneys for Appellant

JOHN L. MAXEY II*
304 North Congress Street
Post Office Box 22666
Jackson, Mississippi 39205
(601) 355-1553

EDWIN LLOYD PITTMAN,
Attorney General
FRANK SPENCER
W. GLENN WATTS

Attorneys for Appellee State of Mississippi ex rel.
Edwin Lloyd Pittman, Attorney General

JESSE C. PENNINGTON*
Post Office Box 22887
Jackson, Mississippi 39205
(601) 944-0765

LEWIS BURKE
Central Mississippi Legal
Services

Attorneys for Appellee Mississippi Legal Services Coalition

*Counsel of Record

APPEAL DOCKETED JUNE 10, 1987
JURISDICTION POSTPONED OCTOBER 5, 1987

2 cop

TABLE OF CONTENTS

STATEMENT OF OMITTED MATERIALS

The following opinions, orders, and other materials have been omitted in printing this appendix because they appear on the following pages in the Appendix to the Jurisdictional Statement:

CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

DOCKET OF THE MISSISSIPPI PUBLIC SERVICE COMMISSION

Date	Proceedings
November 16, 1984	Application for Rate Increase filed
November 16, 1984	Order of Suspension—Not Less Than 120 Days
November 16, 1984	Order employing Special Counsel
November 16, 1984	Order employing Special Consultant
November 20, 1984	Motion of Mississippi Legal Services Coalition in Opposition to the Application of Mississippi Power & Light Company for Waiver of Filing Requirements
November 20, 1984	Notice of Intervention of Mississippi Legal Services Coalition
November 28, 1984	Notice of Intervention of Attorney General
November 29, 1984	Notice of Appearance of Mississippi Legal Services Coalition
November 29, 1984	Motion of Mississippi Legal Services Coalition to Dismiss or for a Stay of the Proceedings
December 3, 1984	Notice of Motion—Motion to Dismiss January 2, 1985

Date	Proceedings
December 4, 1984	Order setting Schedule
December 5, 1984	Notice of Intervention filed
December 6, 1984	Order for Pre-Hearing
December 12, 1984	International Paper Company Request for Leave to Intervene
December 17, 1984	Staff Report to the Commission
December 19, 1984	Data Request of Mississippi Legal Services Coalition
December 19, 1984	Petition of General Motors Corporation for Leave to Intervene
December 19, 1984	Amended Order employing Special Consultant
December 27, 1984	Amended Motion of Mississippi Legal Services Coalition in Opposition to the Application of Mississippi Power & Light Company for Waiver of Filing Requirements and Its Amended Motion to Dismiss, or in the Alternative, for a Stay of the Proceedings
December 27, 1984	Uncle Ben's Foods, Inc., Request for Leave to Intervene
December 28, 1984	Notice of Intervention of United Gas Pipe Line Company

Date	Proceedings
December 28, 1984	Response of Mississippi Power & Light Company to Motion of Mississippi Legal Services Coalition in Objection to Motion for Waiver of Filing Requirements
December 28, 1984	Response of Mississippi Power & Light Company to the Amended Motion to Dismiss, or in the Alternative, for a Stay of Proceedings filed by Mississippi Legal Services Coalition
December 28, 1984	Motion to Dismiss Mississippi Power & Light Company's Rate Increase Request and Conduct Special Investigations
January 3, 1985	Intervention in Protest of City of Jackson (Petition)
January 3, 1985	Order setting Special Hearing for January 15, 1985 on Motion of Mississippi Legal Services Coalition and Attorney General to Dismiss Cause
January 4, 1985	Notice of Intervention of Southern Cotton Ginners Assn.
January 4, 1985	Notice of Intervention on Behalf of Resident Holders of Security Interests
January 7, 1985	First Data Request of International Paper Company to Mississippi Power & Light Company

Date	Proceedings
January 7, 1985	First Data Request of General Motors Corporation to Mississippi Power & Light Company
January 8, 1985	Notice of Suspension—Waived 20-Day Notice
January 8, 1985	Order setting Hearing on Interim Rates
January 11, 1985	General Motors Corporation—Special Data Request No. 1
January 11, 1985	Designation of Testimony and Portions of Filing Which Support Interim Rates for Independence Unit 2; Testimony of Frank S. York, Jr., Frank F. Gallaher, Jr., and Howard E. Lubow
January 14, 1985	Amended Order setting Schedule
January 14, 1985	Testimony & Exhibits of John B. Legler
January 14, 1985	Direct Testimony of Hugh Larkin, Jr.
January 15, 1985	Testimony of Thomas H. Weiss
January 15, 1985	Testimony of John E. Warren
January 15, 1985	Order denying Motion of Mississippi Legal Services Coalition in Opposition to the Application of Mississippi Power & Light Company for Waiver of Filing Requirements

Date	Proceedings
January 15, 1985	Order denying Motion of Mississippi Legal Services Coalition to Dismiss, or in the Alternative, for a Stay of the Proceedings
January 15, 1985	Order allowing Withdrawal of Motion of Attorney General to Dismiss
January 17, 1985	Amended Order of Suspension
January 17, 1985	Compliance With Rule 6E-"Notice of Customers"
January 17, 1985	Order setting Interim Rates
February 5, 1985	Revised Amended Order setting Schedule
February 21, 1985	Order granting Staff Access and Right to Inspect and Examine All Accounts, Records, Etc., of Mississippi Power & Light Company
March 5, 1985	Order severing Rate Design and Prudency
April 15, 1985	Statement of Carl G. Brooking
April 15, 1985	Statement of Dr. Cyrus C. Johnson
April 15, 1985	Testimony of William C. Burnley, Jr.
April 15, 1985	Testimony of Don Richardson
April 15, 1985	Testimony and Exhibits of Thomas H. Weiss
April 15, 1985	Testimony of Dr. E. E. Thrash

Date	Proceedings
April 15, 1985	Testimony of Willie L. Rose
April 15, 1985	Testimony of Dr. Mark N. Cooper
April 15, 1985	Testimony of Maurice Brubaker
April 16, 1985	Testimony of Lay Witnesses on Behalf of Mississippi Legal Services Coalition
April 22, 1985	Petition of Georgia-Pacific Corporation for Leave to Intervene
May 1, 1985	Stipulation
May 1, 1985	Order changing Hearing from May 20 to May 21
May 1, 1985	Motion of Mississippi Power & Light Company to Strike Portions of Pre-Filed Testimony of Dr. Mark N. Cooper
May 1, 1985	Motion of Mississippi Power & Light Company to Strike Portions of Pre-Filed Direct Testimony of Thomas H. Weiss
May 1, 1985	Motion of Mississippi Power & Light Company to Strike Portions of Pre-Filed Testimony of Staff Witnesses Larkin and Dittmer
May 2, 1985	Amended Page Twenty-Seven of Dr. Mark N. Cooper's Pre-Filed Testimony, and Amended Schedule Six
May 6, 1985	Office of Attorney General—Amended Testimony and Exhibits Not Necessary Due to Stipulation Submitted April 30, 1985

Date	Proceedings
May 6, 1985	Statement of Mississippi Power & Light Company of Final Exhibits, Prepared Testimony and Evidence Pursuant to Section 77-3-39 (4) Mississippi Code of 1972, as Amended
May 6, 1985	Response of Georgia-Pacific Corporation to Stipulation
May 6, 1985	Response of General Motors Corporation to Stipulation
May 7, 1985	Motion of Mississippi Legal Services Coalition in Opposition to Mississippi Power & Light Company's Motion to Strike Portions of the Pre-Filed Testimony of Dr. Mark N. Cooper
May 7, 1985	Order accepting and adopting Stipulation
May 8, 1985	Motion of Mississippi Legal Services Coalition for Clarification of Procedure
May 9, 1985	Order denying Motion to Strike Portions of Pre-Filed Direct Testimony of Public Utility Staff Witnesses Hugh Larkin, Jr., and James R. Dittmer

Date	Proceedings
May 9, 1985	Order denying Motion of Mississippi Power & Light Company to Strike Portions of Pre-Filed Testimony of Dr. Mark N. Cooper
May 9, 1985	Order denying Motion to Strike Portions of the Pre-Filed Direct Testimony of Attorney General's Witness Thomas H. Weiss
May 13, 1985	Rebuttal Testimony of Thomas H. Weiss on Behalf of the State of Mississippi Office of the Attorney General
May 13, 1985	Reservation of Rights filed by Mississippi Power & Light Company
May 13, 1985	Rebuttal Testimony of Frank F. Gallaher, James W. Schimpf, William K. Edwards, Regis G. Trumps, E. Eugene Brown, Glenn E. Harder, Howard E. Lubow, John E. Ward, and Lewis J. Perl
May 16, 1985	Page 4-11 of John E. Ward Rebuttal Testimony Void—Replaced with Page 4-11/R
May 20, 1985	Motion of Mississippi Power & Light Company to Strike Portions of Rebuttal Testimony of Thomas H. Weiss
May 20, 1985	Order clarifying Procedure—and Procedural History

Date	Proceedings
June 14, 1985	Final Order
June 21, 1985	Notice of Filing New and Revised Tariffs, Rates, and Charges in Conformity with a Portion of the Commission's Order of June 14, 1985, and Request for Approval Thereof
June 24, 1985	Order approving New and Revised Tariffs, Rates, and Charges in Conformity with a Portion of the Commission's Final Order of June 14, 1985
June 27, 1985	Application of Mississippi Power & Light Company for a Rehearing of a Portion of the Commission's Final Order of June 14, 1985, Pursuant to Section 77-3-65 Miss. Code Ann. (Supp. 1984)
July 2, 1985	Opposition of Mississippi Legal Services Coalition to the Application of Mississippi Power & Light Company for a Rehearing of a Portion of the Commission's Final Order of June 14, 1985, Pursuant to Section 77-3-65 Miss. Code Ann. (Supp. 1984)
July 2, 1985	Order granting Application of Mississippi Power & Light Company for a Rehearing of a Portion of the Commission's Final Order of June 14, 1985, Pursuant to Section 77-3-65 Miss. Code Ann. (Supp. 1984)

Date	Proceedings
July 2, 1985	Order establishing Date for Interim Rehearing and Procedural Schedule
July 8, 1985	Motion of Mississippi Legal Services Coalition to Reconsider the Order Granting Application of Mississippi Power & Light Company for a Rehearing of a Portion of the Commission's Final Order of June 14, 1985, Pursuant to Section 77-3-65 Miss. Code Ann. (Supp. 1984)
July 8, 1985	Rehearing Testimony of Frank S. York, Jr., Frank F. Gallaher, Jr., Edwin A. Lupberger, Howard E. Lubow, E. Eugene Brown, and James W. Schimpf
July 9, 1985	Amended Order establishing Date for Consideration of Settlement Proposal and Procedural Schedule
July 26, 1985	Application for Temporary Emergency Rates Pursuant to Miss. Code Ann. 77-3-41 (Supp. 1984)
August 6, 1985	Order establishing Date for Hearing and waiving 20-day Notice (Aug. 12, 1985)
August 22, 1985	Filing of Mississippi Power & Light v. MPSC in the United States District Court—Civil Action No. J85-0792

Date	Proceedings
August 22, 1985	Order setting Rehearing for October 14, 1985 and directing Mississippi Power & Light Company to Pre-File All Testimony and Exhibits No Later Than September 15, 1985, and All Intervenors to File All Testimony and Exhibits No Later Than September 30, 1985
August 23, 1985	Filing in U.S. District Court—Defendant's Motion for Extension of Time to File Motion to Dismiss and Opposition to Preliminary Injunction and for Additional Time before These Matters Are Set for Hearing
August 29, 1985	Rebuttal Brief of Mississippi Power & Light Company (Civil Action No. J85-0792)
September 4, 1985	September 1985 Rehearing: Testimony of Frank S. York, Jr., E. Eugene Brown, Frank F. Gallaher, Jr., James W. Schimpf, and Howard E. Lubow
September 5, 1985	Resolution from City of Ruleville Opposing Rate Increase
September 10, 1985	Motion of Mississippi Legal Services Coalition for Leave to Intervene
September 16, 1985	Final Order on Rehearing

Date	Proceedings
September 18, 1985	Notice of Filing of Rider Schedules Pursuant to Final Order on Rehearing by Mississippi Power & Light Company
September 19, 1985	Order approving New and Revised Rider Schedules MSE-3, MSE-4 (Revised) and RM-3 (Revised) in Conformity with the Commission's Final Order on Rehearing of September 16, 1985
September 19, 1985	Objection of Attorney General to Rates filed by Mississippi Power & Light Company
October 16, 1985	Notice of Appeal by Mississippi Legal Services Coalition
October 16, 1985	Notice of Appeal by Attorney General to the Mississippi Supreme Court
October 24, 1985	Certificate as to Costs filed by Mississippi Legal Services Coalition
November 5, 1985	Stipulation Pursuant to Section 77-3-39 (7) Miss. Code Ann. (Supp. 1985)
November 6, 1985	Notice of Intervention and Motion of Attorney General to Consolidate Appeals
December 13, 1985	Appeal Record filed with Mississippi Supreme Court

Date	Proceedings
February 25, 1987	No. 56,762 decided in the Mississippi Supreme Court
March 13, 1987	Order revoking Bonding Arrangements
March 18, 1987	Petition of the Mississippi Public Service Commission for Rehearing on Order Vacating and Setting Aside Order of Public Service Commission Entered on March 13, 1987, or Motion for Order Setting Adequate and Sufficient Bond by this Court filed in the Mississippi Supreme Court
March 18, 1987	Brief of Mississippi Public Service Commission in Support of Petition for Rehearing on Order Vacating and Setting Aside Order of Public Service Commission Entered on March 13, 1987, or Motion for Order Setting Adequate and Sufficient Bond by this Court
May 26, 1987	Petition of Attorney General to Roll Back the Authorized Rates of Mississippi Power & Light Company to the Rate Levels in Effect Prior to the Commission's Final Order on Rehearing of September 16, 1985

Date	Proceedings
May 26, 1987	Response of Mississippi Power & Light Company to Petition to Roll Back Rates and Request for Hearing
May 26, 1987	Order setting Refunding Plan

DOCKET OF THE MISSISSIPPI SUPREME COURT

Date	Proceedings
October 16, 1985	Notice of Appeal of State of Mississippi Attorney General
October 23, 1985	Notice of Appeal by Way of Intervention of Mississippi Legal Services Coalition
November 14, 1985	Appearance of Mississippi Power & Light Company as an Appellee
November 19, 1985	Appearance of Resident Security Owners as an Appellee or, in the Alternative, Request for Permission to Appear as an Appellee
November 27, 1985	Order allowing Mississippi Power & Light Company and Resident Security Owners to Appear as Additional Appellees
December 11, 1985	Order granting Motion of Appeal by Way of Intervention of Mississippi Legal Services Coalition

Date	Proceedings
December 20, 1985	Twelve Volumes of Exhibits filed
January 13, 1986	Motion for Time filed
February 28, 1986	Motion of Mississippi Power & Light Company to Advance on the Docket filed
March 7, 1986	Response to Motion to Advance filed
March 17, 1986	Assignment of Error filed by Mississippi Legal Services Coalition
March 17, 1986	Abstract filed
March 17, 1986	Brief of Mississippi Legal Services Coalition filed
March 17, 1986	Seven Assignments of Error filed by State of Mississippi
March 17, 1986	Brief of State of Mississippi filed
June 6, 1986	Appellee's Supplemental Abstract filed
June 6, 1986	Joint Brief of Mississippi Power & Light Company and Resident Security Owners filed
June 6, 1986	Two-Volume Appendix to Brief of Appellees filed
June 6, 1986	Brief of Mississippi Public Service Commission filed

Date	Proceedings
June 25, 1986	Letter and Attachment of Supplemental Citation to Joint Brief for Appellees Mississippi Power & Light Company and Resident Security Owners filed
June 26, 1986	Joint Rebuttal Brief of Appellants filed
August 13, 1986	Order granting Motion to Advance on the Docket
September 11, 1986	Citations of Authority filed by State of Mississippi
September 25, 1986	Response to Citation of Authority filed by Mississippi Power & Light Company
November 11, 1986	Suggestion of Diminution of Record filed by State of Mississippi
November 17, 1986	Response to Suggestion of Diminution of Record filed
November 21, 1986	Response to Suggestion of Diminution of Record filed
December 19, 1986	Suggestion of Diminution of Record filed by Mississippi Power & Light Company
December 19, 1986	Suggestion of Diminution of Record filed by State of Mississippi
December 31, 1986	Response of State of Mississippi to Suggestion of Diminution filed

Date	Proceedings
January 2, 1987	Response of Mississippi Power & Light Company to Suggestion of Diminution of Record filed
January 7, 1987	Additional Citations of Authority filed
January 7, 1987	Order denying Suggestions of Diminution of Record filed December 19, 1986 by Mississippi Power & Light Company and by State of Mississippi
January 8, 1987	Motion to Reschedule Oral Argument filed by State of Mississippi
January 8, 1987	Order granting State of Mississippi's Suggestion of Diminution of Record as filed on November 11, 1986 as to all material except newspaper articles
January 8, 1987	Order denying Motion to Reschedule Oral Argument
January 12, 1987	Oral Argument before the Mississippi Supreme Court
February 25, 1987	Opinion issued by the Mississippi Supreme Court
March 10, 1987	Motion for Stay of Mandate and Brief in Support filed by Mississippi Power & Light Company

Date	Proceedings
March 10, 1987	Petition for Rehearing filed by Mississippi Power & Light Company
March 10, 1987	Motion of System Energy Resources, Inc. and Middle South Utilities, Inc. to Intervene on Petition for Rehearing and to Shorten Time for Appellants to Respond to Motion filed
March 10, 1987	"Proposed" Petition for Rehearing filed
March 16, 1987	Petition of Mississippi Power & Light for a Remedial Writ Setting Aside Order and Vacating or Enjoining Enforcement of Mississippi Public Service Commission Order filed
March 16, 1987	Order vacating and setting aside Order of Mississippi Public Service Commission entered on March 13, 1987
March 18, 1987	Petition for Rehearing filed by Resident Security Holders
March 18, 1987	Petition for Rehearing filed by Mississippi Public Service Commission
March 20, 1987	Response of Mississippi Legal Services Coalition in Opposition to Motion of System Energy Resources, Inc. and Middle South Utilities, Inc. to Intervene on Petitions for Rehearing filed

Date	Proceedings
March 20, 1987	Response of Mississippi Legal Services Coalition in Opposition to Mississippi Power & Light Company's Motion for Stay of Mandate filed
March 23, 1987	Response of State of Mississippi to Motion of System Energy Resources, Inc. and Middle South Utilities, Inc. to Intervene on Petition for Rehearing filed
March 23, 1987	Response of State of Mississippi in Opposition to Motion for Stay of Mandate filed
March 23, 1987	Response of Mississippi Power & Light Company to Motion for Order Setting Adequate and Sufficient Bond
April 20, 1987	Reply to Petition for Rehearing of Mississippi Public Service Commission filed
April 29, 1987	Supplemental Affidavit in Support of Motion for Stay of Mandate filed by Mississippi Power & Light Company
April 29, 1987	Response of Mississippi Public Service Commission to Reply to Petition for Rehearing filed

Date	Proceedings
May 20, 1987	Order denying Petition for Rehearing of Mississippi Power & Light Company and Resident Security Holders, denying Motion of System Energy Resources, Inc. and Middle South Utilities, Inc. to Intervene on Petition for Rehearing and to Shorten Time for Appellants to Respond to Motion, and denying Motion of Mississippi Power & Light Company for Stay of Mandate
May 20, 1987	Notice of Appeal to Supreme Court of the United States filed
May 22, 1987	Mandate issued
June 3, 1987	Copy of Letter from U.S. Supreme Court Clerk to Rex E. Lee Advising that U.S. Supreme Court Has Granted Application for Stay of Judgment Pending Timely Filing and Disposition of Appeal and Conditioned upon the Posting of a Good and Sufficient Bond, in Manner and Amount to Be Determined by the Supreme Court of Mississippi
June 5, 1987	Bond Proposals filed by Parties
June 11, 1987	Order setting Bond

Date	Proceedings
June 18, 1987	Petition for Remedial Writ granting Motion for Mandatory Temporary Restraining Order filed
June 19, 1987	Order granting Mandatory Temporary Restraining Order and Setting Aside Chancery Court Order of June 18, 1987
June 22, 1987	Notice of Appeal to United States Supreme Court
June 30, 1987	Copy of Letter from U.S. Supreme Court to Rex E. Lee with Copy of Order Staying Mississippi Supreme Court Order of June 19, 1987
September 14, 1987	Motion of Mississippi Power & Light Company for Approval of Bonding Requirements
September 17, 1987	Order approving Bonding Requirements

[THIS PAGE INTENTIONALLY LEFT BLANK]

IN THE SUPREME COURT OF THE UNITED STATES
ORDERS ISSUED OCTOBER 5, 1987

* * *

86-1970 Mississippi Power & Light Co. v. Mississippi, etc., et al.

Further consideration of the question of jurisdiction is postponed to the hearing of the case on the merits.

* * *

APPELLANT'S BRIEF

QUESTION PRESENTED

Whether *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986), the Federal Power Act, and the Commerce Clause require a state regulatory commission, in setting retail electric rates, to recognize expenses incurred under FERC wholesale rate decisions that allocate interstate wholesale costs as "a reasonably incurred operating expense"?

PARTIES BELOW

The appellants below were the State of Mississippi ex rel. Edwin Lloyd Pittman, Attorney General of Mississippi, and the Mississippi Legal Services Coalition.

The appellees were Mississippi Power & Light Company, Mississippi Resident Security Owners, and the Mississippi Public Service Commission.

RULE 28.1 STATEMENT

Mississippi Power & Light Company ("MP&L") is a wholly-owned subsidiary of Middle South Utilities, Inc. Middle South Utilities, Inc. has no parent company. Its other wholly-owned subsidiaries are Arkansas Power & Light Company ("AP&L"), Louisiana Power & Light Company ("LP&L"), New Orleans Public Service Inc. ("NOPSI"), System Energy Resources, Inc. (formerly named Middle South Energy, Inc.), MSU System Services, Inc. (formerly named Middle South Services, Inc.), and Electec, Inc. In addition, AP&L, LP&L, MP&L, and NOPSI jointly own the common stock of System Fuels, Inc., and AP&L owns the common stock of Associated Natural Gas Company.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Other Authorities

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

APPELLANT'S BRIEF

OPINIONS BELOW

The opinion of the Supreme Court of Mississippi, dated February 25, 1987 (Appendix to Jurisdictional Statement, 1a-23a ("J.S. App.")), is reported at 506 So. 2d 978 (1987), and its decision denying rehearing, dated May 20, 1987 (J.S. App. 197a-198a) is unreported. The Final Order on Rehearing of the Mississippi Public Service Commission, dated September 16, 1985 (J.S. App. 25a-59a) is unreported. The decisions of the Federal Energy Regulatory Commission ("FERC") that establish the wholesale power and cost allocations and rates that are at issue in this appeal are reproduced in the Appendix to Jurisdictional Statement: FERC Opinion No. 234 (J.S. App. 73a-152a), which is reported at 31 FERC (CCH) ¶ 61,305 (1985), and FERC Opinion No. 234-A (J.S. App. 153a-195a), which is reported at 32 FERC (CCH) ¶ 61,425 (1985).

JURISDICTION

The judgment of the Mississippi Supreme Court upholding the validity of a Mississippi statute, *Miss. Code Ann.* § 77-3-39 (Supp. 1986), was issued February 25, 1987. MP&L's timely petition for rehearing was denied on May 20, 1987. MP&L filed a Notice of Appeal on May 20, 1987 (J.S. App. 201a-202a) and a Jurisdictional Statement on June 8, 1987. On October 5, 1987, this Court entered an order postponing consideration of jurisdiction until the hearing on the merits. Joint Appendix ("App.") 23. This Court has jurisdiction under 28 U.S.C. § 1257(2). *See* pp. 26-31, *infra*.

CONSTITUTIONAL AND STATUTORY PROVISIONS

The United States Constitution, Article VI, Clause 2: "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land . . . ."

The United States Constitution, Article I, Section 8, Clause 3: "The Congress shall have Power . . . [t]o regulate Commerce . . . among the several States . . . ."

The pertinent provisions of the Federal Power Act, 16 U.S.C. §§ 791a–828c, and of the Mississippi Code, §§ 77-3-37, 77-3-39, are reprinted at pages 61a–68a and 69a–71a, respectively, of the Appendix to Jurisdictional Statement.

STATEMENT OF THE CASE

Introduction

This appeal presents the question that was decided in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986): whether the costs incurred under the FERC rate schedules that allocate interstate wholesale costs among affiliated utilities must be treated as "a reasonably incurred operating expense" in setting retail electric rates.

Like *Nantahala*, this case arises from the fact that electricity has widely varying costs of production. Older oil and gas-fired, coal-fired, hydroelectric, and nuclear generating plants produce electricity at a lower average cost than do nuclear plants completed in the aftermath of the 1979 Three Mile Island accident and the high interest rates of that period. Each type of generating capacity serves consumer demand in the nation today. At the same time, each individual state would naturally prefer to have allocated to its citizens as little of the high-cost capacity and as much of the low-cost capacity as possible. Under the Federal Power Act, FERC has exclusive jurisdiction to make these wholesale cost allocations among affiliated as well as unaffiliated public utilities that pool and exchange electricity.

Here, FERC conducted massive proceedings to determine how low-cost and high-cost electricity should be allocated to produce "just and reasonable rates" under which Mississippi Power and Light Company ("MP&L") and the other utilities that comprise the Middle South System acquire electricity. The Mississippi Attorney General, the Mississippi Public Service Commission ("Mississippi PSC"), and other Mississippi entities unsuccessfully urged FERC to prescribe wholesale rates under which Mississippi retail ratepayers would be allocated none, or little, of the costs of the recently-constructed Grand Gulf 1 nuclear plant. Similar efforts were made on behalf of other states served by the Middle South System. FERC rejected these efforts and prescribed wholesale rates under which MP&L is allocated 33% of the higher-cost Grand Gulf 1 capacity and thus uses correspondingly less of the Middle South System's lower-cost capacity.

The Mississippi PSC thereupon set retail rates that give effect to these FERC rate schedules and allow MP&L to recover the Grand Gulf 1 expenses that FERC requires MP&L to incur. After this rate increase, the electric bills of MP&L customers have continued to be below the average in the nation.

The Mississippi Attorney General and the other appellee in this case appealed this retail rate decision and challenged the reasonableness of MP&L's Grand Gulf 1 expenses on the very grounds that FERC had rejected. The Mississippi Supreme Court set aside the retail rate increase, holding that Mississippi law prohibits MP&L from recovering any of these federally-prescribed Grand Gulf 1 costs unless and until the Mississippi PSC first determines the "prudence" of MP&L's Grand Gulf 1 cost allocation. This holding violates the Federal Power Act and the Commerce Clause.

I. MP&L And The Middle South System.

MP&L is a utility that provides retail electric service to approximately 333,000 customers in the western half of Mississippi. MP&L is a wholly-owned subsidiary of Middle South Utilities, Inc. ("MSU"), which is a public utility holding company under the Public Utility Holding Company Act, 15 U.S.C. §§ 79a, *et seq.* MSU has three other operating electric utility subsidiaries that serve retail customers: Arkansas Power and Light Company ("AP&L"), Louisiana Power and Light Company ("LP&L"), and New Orleans Public Service Inc. ("NOPSI"). The four Middle South operating companies serve retail customers in four states—Mississippi, Louisiana, Arkansas, and Missouri—and the retail rates of these companies are regulated by five different state or local regulatory authorities.[1] MP&L alone is regulated by the Mississippi PSC.

The four Middle South operating companies and MSU's subsidiary, Middle South Energy, Inc. ("MSE")[2] form a highly

[1]AP&L is regulated by the Arkansas Public Service Commission and the Missouri Public Service Commission; LP&L is regulated by the Louisiana Public Service Commission and, with respect to one ward of the City of New Orleans, the Council of the City of New Orleans; NOPSI is regulated by the Council of the City of New Orleans; and MP&L is regulated by the Mississippi PSC.

[2]MSE owns and operates Grand Gulf 1. MSE was renamed System Energy Resources, Inc. in 1986.

integrated network for the transmission and sale of electricity in interstate commerce: the Middle South System. As required by the Public Utility Holding Company Act, these companies are integrated electrically and are "operated as a single interconnected and coordinated system" serving a single geographic region. *See* 15 U.S.C. §§ 79b(a)(29), 79k(b). Thus, although MP&L and each other MSU operating company separately owns some generating capacity, all this generation is "pooled." A single control facility in Pine Bluff, Arkansas centrally dispatches all the generating facilities on the system, without regard to ownership, to provide energy at the lowest reasonable cost in the system as a whole.

The arrangements among the companies for the transmission, sale, and exchange of electricity have been governed by a series of power pool agreements ("System Agreements") that are filed with, and subject to, the exclusive jurisdiction of the Federal Energy Regulatory Commission ("FERC").[3] These System Agreements determine how the Middle South operating companies share the costs of electric capacity[4] and electric energy.[5]

[3]The original System Agreement was filed at FERC in 1951. A significantly revised System Agreement was filed and made effective in 1973, and was approved by the FERC, as modified, in *Middle South Services, Inc.*, 16 FERC (CCH) ¶ 61,101 (1981), *aff'd sub nom. Louisiana Public Service Commission* v. *FERC*, 688 F.2d 357 (5th Cir. 1982), *cert. denied*, 460 U.S. 1082 (1983). A new System Agreement and related contracts that are central to this case were filed in 1982. *See* pp. 10-13, *infra*.

[4]"Capacity" is the amount of electric energy available from a generating unit or facility at any one time. A system must have capacity that exceeds "peak" demand, plus a reasonable reserve. Capacity is measured in kilowatts. Generation capacity costs are the fixed costs of owning a generation unit or purchasing generation capacity.

[5]"Energy" is the amount of electricity delivered over time; it is measured in kilowatt-hours. Energy costs are the variable costs (e.g., labor and fuel) of each unit of electricity produced by a plant.

In this Brief, "capacity" and "energy" will sometimes be referred to collectively as "power" or "electricity."

The Middle South System adds new generating facilities and capacity as required to meet the growing demand for electricity in the Middle South region. Under each of the System Agreements, the decisions of when and how to add capacity have been made by a system-wide operating committee that is comprised of one representative from each operating company and from MSU. This committee plans for the addition of new capacity to meet the needs of the system as a whole at the lowest cost. Thus, although new generating capacity has (with the exception of Grand Gulf 1) been added by individual operating companies, FERC has found that the centralized planning means that the "individual companies from time to time build larger facilities than are necessary to meet their own native load;" this achieves greater "efficiency, reliability and other economies of scale," and "benefit[s] all the . . . companies by having lower costs and greater reliability." 30 FERC at 65,142; *see* 808 F.2d at 1529.[6]

An inevitable consequence of this centralized planning is that there have been periods of time in which some Middle South operating companies have had more capacity than required to meet the "native" demand of their customers and other Middle South companies have had less capacity. The System Agreements

[6]Four different FERC opinions have addressed the FERC allocation and wholesale rate determinations that are central to this case: *Middle South Energy, Inc.*, 26 FERC (CCH) ¶ 63,044 (1984) (Administrative Law Judge Liebman); *Middle South Services, Inc.*, 30 FERC (CCH) ¶ 63,030 (1985) (Administrative Law Judge Head); *Middle South Energy, Inc.*, FERC Opinion No. 234, 31 FERC (CCH) ¶ 61,305 (1985) (J.S. App. 73a-152a); FERC Opinion 234-A, 32 FERC (CCH) ¶ 61,425 (1985) (J.S. App. 153a-195a). These will be cited as "___ FERC at ___."

These FERC opinions were reviewed in the comprehensive opinion of the United States Court of Appeals for the District of Columbia Circuit in *Mississippi Industries v. FERC*, 808 F.2d 1525, *modified on rehearing*, 822 F.2d 1104 (D.C. Cir. 1987), *petitions for certiorari pending*, Nos. 86-1380, 86-1424, and 87-469. It will be cited as "808 F.2d at ___."

have assured that the manner and order in which new capacity is added do not produce gross differences in the generating costs of the individual Middle South operating companies. Since 1951, the MSU System Agreements have roughly "equalized" the costs of investing in new capacity among the operating companies by requiring "equalization payments" from operating companies that have less than their share of system capacity ("short companies") to companies that have more than their share ("long companies"). *See* p. 11 n.12, *infra*; 26 FERC at 65,099; 30 FERC at 65,122-23; 808 F.2d at 1529-30. MP&L has been a "long" company during all periods pertinent to this case.

II. Grand Gulf 1.

In the early 1970s, the Middle South System determined that a major addition of new electric capacity would be required to meet the projected increases in demand in its region. At the same time, because the Middle South System had been almost entirely dependent on gas and oil-fired generating facilities—the fuel costs of which had been escalating rapidly—Middle South made a system decision to diversify its fuel sources by adding nuclear and coal-fired generation and reducing the system's dependence on oil and natural gas.

As part of this effort, the Middle South System decided to finance, construct, and operate a nuclear-fueled generating station near Port Gibson, Mississippi (Grand Gulf 1) to meet the projected demand of the system as a whole. 31 FERC at 61,653-54; J.S. App. 118a-120a. As FERC found, the information available at the time showed that construction and completion of Grand Gulf 1 would produce savings for all the companies of the Middle South System. 26 FERC at 65,101-02; 31 FERC at 61,651-54 (J.S. App. 115a-120a). Grand Gulf 1 was originally planned as an MP&L project, but neither MP&L nor any other individual MSU operating company had the resources to finance this project. Thus, in 1974, MSU formed a new subsidiary, Middle South Energy, Inc. ("MSE") to finance, construct, and operate Grand

Gulf 1. *Id.* In 1974, the Mississippi PSC granted a certificate of convenience and necessity that authorized construction of Grand Gulf 1 in Mississippi; this order recognized that the allocation of Grand Gulf 1's capacity and energy among the Middle South operating companies was subject to FERC regulation.[7]

Grand Gulf 1 was substantially more expensive to complete than had been originally projected, its costs per kilowatt of capacity having increased from the some $500 per kilowatt that had been estimated in 1974, to the some $2500 per kilowatt estimated for 1985. 26 FERC at 65,103; 808 F.2d at 1531-32 & nn.16-18. Grand Gulf 1's capacity costs, however, are comparable to those of other nuclear plants completed in the aftermath of the 1979 accident of Three Mile Island[8] and lower than those of subsequently completed plants.[9] The combination of the resulting regulatory delays, the new construction and design requirements imposed by the Nuclear Regulatory Commission, and the high interest and carrying costs during this period radically increased the costs of completing all such plants. 26 FERC at 65,103; *see* n.8, *supra*.

[7]The Mississippi PSC Order that grants this certificate refers to the fact that the 1973 System Agreement had, at that time, been filed with FERC, but had not yet been approved. *Compare* Appendix to Mississippi's Motion to Dismiss, pp. 32-33, *with* p. 5 n.3, *supra*.

[8]This was the finding of a 3-volume Grand Gulf construction audit ordered by the Mississippi PSC and released in July, 1985. It concluded that "[f]actors causing major cost escalation and schedule slippage were industry-wide in nature" and that the cost and schedule of the plant "compare adequately against those of similar nuclear units constructed during the same time frame." *Grand Gulf Construction Audit*, Executive Summary, Findings and Conclusions, p. 3 (April, 1985). *See also* n.9, *infra*. This audit assumed a cost per kilowatt of $2739.

[9]TVA has found that Grand Gulf 1 has lower capital costs per kilowatt than 16 of 22 nuclear plants scheduled to begin commercial operations in 1985 or thereafter and that these nuclear plants have total construction costs (including interest during construction) as high as $5800 per kilowatt. Tennessee Valley Authority, Office of Nuclear Power, *U.S. Nuclear Plants Cost Per KW Report*, pp. A, B (March, 1987).
(Footnote continued on next page)

Nonetheless, MSE completed Grand Gulf 1.[10] As FERC found, it had continued to appear that Grand Gulf 1 would produce electricity at a lower average cost per kilowatt hour than would alternative gas and oil-fired generating facilities—the fuel prices of which had dramatically escalated in the 1970s and early 1980s. 26 FERC at 65,112-13. In any event, because nuclear plants are, once constructed, far cheaper to operate than fossil fuel plants (*see* J.S. App. 6a),[11] completing Grand Gulf 1 and operating it was, at that time, far more economical than relying on existing oil and gas-fired facilities. R. 1637-39; 26 FERC at 65,112-13.

The Middle South System's shift to nuclear and coal-fired generating facilities and the "unforeseen developments" of the late 1970s resulted, in the District of Columbia Circuit's words, in the "collapse of the investment equalization program" that the system had followed since 1951. 808 F.2d at 1531. This program had achieved its objective of "roughly equalizing" the generation

(Footnote continued from previous page)

Similarly, the Department of Energy has found that the seven nuclear plants that began service in 1985 had average construction costs of $2466 per kilowatt, that the eight plants completed in 1986 had average construction costs of $2765 per kilowatt, and that the thirteen plants expected to begin operations in 1987 had average estimated capacity costs of $3776 per kilowatt. Department of Energy, Energy Information Administration, *Nuclear Power Plant Construction Activity, 1986*, p. 13 & Table 4 (July 24, 1987). Grand Gulf 1's actual construction cost per kilowatt turned out to be $2933 when commercial operation began.

[10]At the same time, because it became clear in the late 1970s that the actual growth in demand in the Middle South region was falling short of prior projections, Middle South cancelled other planned generating facilities. *See* R. 1637-39; *see also* 26 FERC at 65,120-22. Grand Gulf 1's capacity was still projected to produce savings for the system operating companies, so Grand Gulf 1 was completed.

[11]Indeed, because nuclear plants are far less expensive to operate than fossil fuel plants and because energy costs include only the variable costs of operation (*see* p. 5 n.5, *supra*), the energy provided by Grand Gulf 1 and other MSU nuclear plants is the lowest cost energy on the Middle South System. Each of the Middle South companies' costs increase when Grand Gulf 1 is shut down for periodic maintenance.

costs of the Middle South companies from the 1950s through the 1970s for one reason: the total generation costs of each fossil fuel and nuclear generating facility on the system had been comparable throughout this period. 30 FERC at 65,168; 808 F.2d at 1530-31. Due to the cost disparities between nuclear and non-nuclear generating capacity that arose in the 1980s, a new method had to be developed to eliminate gross differences in the generation costs of the four Middle South operating companies.

III. The FERC Proceedings.

In 1982, the Middle South System companies entered into two new agreements that, in tandem, were designed to correct these problems, to achieve a rough equalization of generation costs among the four operating companies, and to produce "just, reasonable and nondiscriminatory" wholesale rates for each company's acquisition of power. Both of these agreements were filed with FERC as FERC rate schedules.

The first agreement is a Unit Power Sales Agreement ("UPSA") that allocated the costs and capacity of Grand Gulf 1 among the Middle South operating companies, with a 0% allocation for AP&L. UPSA further determines all the other elements of the wholesale rates that MP&L and each operating company pay for Grand Gulf 1 power. It was filed with FERC as MSE FERC Rate Schedule No. 1.

The second agreement is the 1982 System Agreement that replaces the earlier 1973 System Agreement, and that comprises multiple FERC rate schedules. This agreement seeks roughly to equalize generation capacity costs among the Middle South operating companies by requiring the "short" companies to pay the "long" companies for all their capacity in excess of their share of system capacity; those payments are based on the investment

costs of "intermediate" oil and gas-fired generation.[12] Under this Agreement, the determination whether individual companies are "long" or "short" is based on both the capacity of each individual company and also on its share of Grand Gulf 1 under UPSA.

Thus, UPSA and the 1982 System Agreement supplement each other to allocate all the power available to the Middle South System (low-cost as well as high-cost). *See* 808 F.2d at 1540.

FERC instituted two separate dockets to investigate these agreements under Sections 205 and 206 of the Federal Power Act. All recognized that the FERC decision in this wholesale rate proceeding would have "substantial rate impacts" on the Middle South operating companies and their retail customers. *Middle South Energy, Inc.*, 32 FERC (CCH) ¶ 61,207 at 61,478 (1985); *see* 808 F.2d at 1542-43. Thus, representatives of every affected group in each of the four states intervened in these FERC proceedings, including the public utility commissions in each state, other government officials, and customer groups. Each urged the cost allocations and wholesale rates that would be most beneficial to customers in that state. For example, Arkansas and Missouri authorities defended the 0% allocation of Grand Gulf 1 capacity to AP&L, whereas Mississippi, Louisiana, and New Orleans authorities opposed it.

The Mississippi Contentions. The Mississippi PSC, the two appellees in this case (the Mississippi Attorney General and the Mississippi Legal Services Coalition), and other Mississippi enti-

[12]Specifically, each operating company is "responsible" for the same percentage of total Middle South System capacity as that company's percentage of the total system demand, with the "excess" over their pro rata share of system demand subject to equalization payments. As the Court of Appeals for the District of Columbia Circuit stated, the agreement effectively requires the long companies to "contribute their excess capacity to 'short' companies" and to receive, "in return," payments "based on the investment costs of 'intermediate' oil and gas fired generation facilities." 808 F.2d at 1554.

ties extensively participated in these FERC proceedings. They made two related arguments under which MP&L would have received no or little Grand Gulf 1 capacity and proportionately more of the benefits of the System's low-cost capacity.

First, the Mississippi Attorney General, the Mississippi Legal Services Coalition, and the Mississippi PSC each argued that no Grand Gulf 1 capacity should be allocated to MP&L because it does not currently "need" Grand Gulf 1 to meet MP&L's present load. The basis for this argument was that MP&L had, over the years, constructed or acquired more capacity than was needed to serve its native load and that MP&L was projected to be a "long" company for approximately 10 years even without Grand Gulf 1. These Mississippi parties urged FERC to prescribe a modification of the earlier 1973 System Agreement that would make MSE a party to it. The net effect would be that the responsibility for Grand Gulf 1 would be borne entirely by "short" companies and that MP&L would bear none of the Grand Gulf 1 capacity costs until the 1990s; by then, depreciation will have "substantially reduced [Grand Gulf's] costs" and it will thus produce cheaper electricity. 30 FERC at 65,167.

FERC flatly rejected this argument. It found that the allocation that would result would be unjust and discriminatory. 31 FERC at 61,656 n.19 (J.S. App. 124a-125a n.19); 30 FERC at 65,167; 26 FERC at 65,112. It reasoned that the fortuity that MP&L had added other capacity recently cannot permit it to avoid responsibility for generation reasonably constructed to meet the needs of the system as a whole. FERC's finding was unanimously affirmed by the Court of Appeals for the District of Columbia Circuit (808 F.2d at 1564), and no party sought Supreme Court review of this holding.

Second, these Mississippi parties contended that the Mississippi PSC's approval of the construction of Grand Gulf 1 was somehow premised on the ground that FERC wholesale rate schedules

would be put into effect that adopt the foregoing allocation method in which MSE is made a party to the 1973 System Agreement. FERC rejected this argument on the ground that the Mississippi PSC certificate was not conditioned on any particular allocation method and that the Mississippi PSC did not, in any event, have the authority to prescribe any allocation of wholesale costs and capacity among system companies, much less an allocation that FERC finds to be unjust, unreasonable, and discriminatory. 31 FERC at 61,645 (J.S. App. 103a); 30 FERC at 65,166; 26 FERC at 65,111-12. This holding, too, was unanimously affirmed by the Court of Appeals (808 F.2d at 1549-50), and no party sought Supreme Court review of this holding.

In addition, MP&L and other Mississippi parties urged FERC to prescribe an allocation formula under which Mississippi would receive a far lower allocation (approximately 14.5%). 31 FERC at 61,638; J.S. App. 90a-91a. Mississippi parties also advanced a number of other arguments that would have resulted in relatively lesser cost burdens on MP&L, and relatively greater burdens on the other companies. 32 FERC at 61,958-59; J.S. App. 185a-187a. Each of these contentions was rejected by FERC. *Id.*

FERC's Decision. After three years of proceedings, FERC issued its final decisions in FERC Opinions 234 and 234-A in which it addressed the UPSA and 1982 System Agreement together. J.S. App. 73a-152a, 153a-195a. FERC expressly found that Grand Gulf 1 had been planned and completed to meet the needs of the entire Middle South System as a whole (31 FERC at 61,651-57; J.S. App. 115a-126a);[13] that this was part of a

[13]In FERC rate proceedings, all costs are presumed to be prudently incurred and will be included in wholesale rates unless objections are raised to their reasonableness. *Minnesota Power & Light Co.*, 11 FERC (CCH) ¶ 61,312 at 61,645 (1980); *New England Power Co.*, 31 FERC (CCH) ¶ 61,047 (1985), *aff'd sub nom. Violet v. FERC*, 800 F.2d 280 (1st Cir. 1986). In this proceeding, MSE introduced uncontradicted evidence that the decisions to initiate Grand Gulf 1 and to complete

(Footnote continued on next page)

"reasonable" system plan to diversify power sources (*id.*); and that "the costs of Grand Gulf capacity and energy should be shared equitably by all four operating companies and their customers." 31 FERC at 61,632-33; J.S. App. 80a. The question FERC asked, therefore, was "whether the 1982 System Agreement and UPSA, as filed, together will achieve proper cost allocation" and just, reasonable, and nondiscriminatory rates. 31 FERC at 61,655; J.S. App. 122a. FERC held that it would not, because facts and circumstances that arose after the two agreements had been executed rendered them unreasonable and discriminatory. 32 FERC at 61,957; J.S. App. 183a.

FERC considered prescribing alternative cost allocation methods that ranged from equalizing all production costs on the Middle South System to equalizing only the investment costs of Grand Gulf 1. 32 FERC at 61,957-61; J.S. App. 182a-192a. FERC found that the interrelated rate schedules would produce a rough equalization of all generating costs and just and reasonable rates if the investment in all the system's nuclear units were

(Footnote continued from previous page)
construction were reasonable and prudent and that the entire Grand Gulf 1 investment should therefore be included in MSE's rate base. FERC established wholesale rates for MSE that did not exclude any percentage of the Grand Gulf 1 investment from the wholesale rate base and revenue requirements. *See, e.g.*, 26 FERC at 65,101-03; 31 FERC at 61,651-56 (J.S. App. 115a-126a). Moreover, contrary to the Mississippi Supreme Court's statements (J.S. App. 17a), Administrative Law Judge Liebman expressly found that completion of the unit was "prudent":

> "[C]ontinuing construction of Grand Gulf Unit No. 1 was prudent because Middle South's executives believed Grand Gulf would enable the Middle South system to diversify its base load fuel mix and, it was projected, at the same time, [to] produce power for a total cost (capacity and energy) which would be less than existing alternatives on the system."

26 FERC at 65,112-13. This finding was not challenged before FERC or the Court of Appeals.

equalized so that each System operating company shares "the cost of nuclear capacity roughly in proportion to each company's share of System demand." 31 FERC at 61,656; J.S. App. 123a. To achieve this allocation, FERC substantially approved the 1982 System Agreement, but dramatically changed the entitlement percentages of UPSA, as follows:

	UPSA, as filed	Allocation under Opinion No. 234
AP&L	0%	36%
LP&L	38.57%	14%
MP&L	31.63%	33%
NOPSI	29.80%	17%

As FERC stated, the effect of this prescription is "not just to allocate Grand Gulf costs, but to allocate the costs of all nuclear capacity on the MSU system." 31 FERC at 61,633; J.S. App. 81a.

Because UPSA "establishes the rates that" MP&L and each other operating company "will pay to MSE" for Grand Gulf 1 capacity and energy, FERC's decision also determined the other elements of MSE's wholesale rate base and revenue requirements. 31 FERC at 61,657; J.S. App. 126a. FERC accepted the arguments of some parties that certain expenses should be excluded from MSE's wholesale rates, and rejected other such arguments that appellees and other parties in the proceeding had advanced. *See, e.g.*, 31 FERC at 61,657-60 (J.S. App. 126a-132a); 26 FERC at 65,132-49. Because no one challenged the findings that Grand Gulf 1 was reasonably planned and completed to meet the needs of the system as a whole (*see* pp. 13-14 & n.13, *supra*), FERC established wholesale rates that permit MSE to earn a return on 100% of its Grand Gulf 1 investment. FERC has continuing jurisdiction to assure the reasonableness of MSE's Grand Gulf 1 wholesale rates.

Subsequent Federal Proceedings. The Mississippi PSC, the two appellees in this case (the Mississippi Attorney General and the Mississippi Legal Services Coalition), other governmental offi-

cials, MP&L, AP&L, and organizations representing consumer interests in each of the Middle South System states all appealed FERC Opinions 234 and 234-A to the United States Court of Appeals for the District of Columbia Circuit. Earlier this year, that court affirmed the FERC orders in part and reversed them in part. *Mississippi Industries v. FERC*, 808 F.2d 1525, *modified on rehearing*, 822 F.2d 1104 (D.C. Cir. 1987), *petitions for certiorari pending*, Nos. 86-1380, 86-1424, and 87-469.

The Court of Appeals unanimously affirmed FERC's jurisdiction. 808 F.2d at 1539-53. The court further unanimously affirmed FERC's rejection of the arguments of the Mississippi Attorney General, the Mississippi PSC, and the Mississippi Legal Services Coalition under which MP&L would have been allocated none of the Grand Gulf 1 capacity (*id.* at 1563-65) or only that allocation that allegedly was a premise of the earlier Mississippi PSC order authorizing construction of the plant in Mississippi. *Id.* at 1549-50. No party sought Supreme Court review of these holdings. However, on rehearing, the court held that FERC had not adequately explained its reasons for ordering equalization of system nuclear investment costs, and remanded the case to FERC for further proceedings. 822 F.2d at 1105. *See* 808 F.2d at 1568-69.

On July 24, 1987, FERC entered an order that provided that the allocation and rates prescribed in Opinions 234 and 234-A would continue to be the lawful rates until further order of FERC. *System Energy Resources, Inc.*, 40 FERC (CCH) ¶ 61,078 (1987). No party sought review of this order.

On November 30, 1987, FERC issued its decision on remand. FERC there addressed each of the issues raised by the Court of Appeals Opinion and reaffirmed the Grand Gulf 1 cost allocations of FERC Opinions 234 and 234-A.[14]

[14] *System Energy Resources, Inc.*, Dockets Nos. ER82-616-032 & ER82-483-028, Opinion and Order on Remand Reaffirming Prior Allocation, FERC Opinion No. 292 (issued Nov. 30, 1987).

IV. The Mississippi Retail Rate Proceedings.

After Grand Gulf 1 began operating on July 1, 1985, the FERC decisions and rate schedules required MP&L to begin paying about $27 million per month for Grand Gulf 1 capacity—although that amount has declined.[15] Correlatively, the allocation of 33% of Grand Gulf 1 capacity to MP&L increased the amount by which it was a "long" company. Under the 1982 System Agreement, the Middle South operating companies that are "short" became required to pay MP&L, each month, for the entire amount of capacity that MP&L has in excess of its pro rata share of the system capacity, based on the capacity costs of oil and gas-fired generating facilities.[16]

The effect of FERC Opinion 234 was that MP&L needed a retail rate order establishing its right to recover an additional $327 million annually; otherwise, the Mississippi PSC found that MP&L "will quickly become insolvent," J.S. App. 29a. MP&L had filed an application for such an increase with the Mississippi PSC in November, 1984. This application also sought rate relief on other grounds. On June 14, 1985, the Mississippi PSC entered a final order that determined all MP&L's non-Grand Gulf 1

[15] MP&L's monthly bills for Grand Gulf 1 capacity have since declined to about $23 million a month and will decline still further as the plant is further depreciated. MP&L's retail rate schedules flow through all such reductions to retail customers. R.4278-80.

[16] *See* pp. 10-11 & n.12, *supra*. The statement in the Mississippi Supreme Court's opinion that "MP&L admitted at oral argument that it is selling the less expensive energy off the system and retaining the electricity allocated to it from Grand Gulf" (J.S. App. 15a) is a reference to the capacity equalization payments under the 1982 System Agreement. It was possible to so characterize the FERC rate schedules only because FERC approved equalization payments based on the costs of oil and natural gas generation, rather than the costs of nuclear capacity. *See* pp. 10-11 & n.12, *supra*. The Mississippi Supreme Court is incorrect in suggesting (J.S. App. 9a) that MP&L may hereafter be "unable" to "sell" its "excess" capacity; under the FERC rate schedules, other MSU companies are required to pay MP&L for this capacity. *See* p. 11 n.12, *supra*.

expenses and revenue requirements, but that excluded MP&L's Grand Gulf 1 expenses from its operating expenses. *See* Final Order (June 14, 1985).[17]

MP&L petitioned for rehearing. The sole issue in this rehearing proceeding, and in the subsequent appeal, was whether the Grand Gulf 1 expenses constituted a "reasonable operating expense." On September 16, 1985, the Mississippi PSC issued an order, on rehearing, that recognized MP&L's Grand Gulf 1 expenses as allocated by FERC, and allowed MP&L to recover all of them in a separate Grand Gulf 1 retail rate schedule. J.S. App. 27a-53a. To moderate the impact of this increase on retail customers, the Mississippi PSC ordered that it be "phased-in" over a ten-year period, with MP&L required to defer recovery of over half its current Grand Gulf 1 expenses and to recover the deferred amounts over a 40-year period.[18] J.S. App. 43a-52a.

The electric bills of MP&L's customers were lower than the average bills of the privately-owned utilities in the nation before

[17]On April 30, 1985, the parties to this proceeding stipulated to virtually all MP&L's non-Grand Gulf 1 revenue requirements. In the June 14, 1985 Final Order, the Mississippi PSC decided all issues necessary to set retail rates at the levels that it determined would recover all of MP&L's legitimate operating expenses and yield MP&L a fair rate of return on its investment. In that order, however, the Mississippi PSC did not recognize MP&L's Grand Gulf 1 expenses as a legitimate operating expense.

[18]Under the Mississippi PSC order, the deferred amounts are now carried on MP&L's books as a deferred asset, and MP&L is placed under the extraordinary burden of financing more than half of its Grand Gulf 1 costs. J.S. App. 48a-51a. To date, MP&L has been able to borrow sufficient funds to meet its Grand Gulf 1 expenses because the order provides assurance that all of these costs will ultimately be recovered. *See id.* 51a.

The MP&L retail rate schedule and Mississippi PSC order further provide that Mississippi retail rates will be immediately reduced and any other savings flowed through to retail customers to the extent that the Grand Gulf 1 wholesale rates and allocations are hereafter modified to reduce MP&L's Grand Gulf 1 expenses. *See* J.S. App. 51a.

the Mississippi PSC's September 16, 1985 Order, and they have continued to be lower than average since that Order took effect.[19]

The Mississippi Attorney General and the Mississippi Legal Services Coalition appealed the Mississippi PSC's September 16, 1985, order to the Mississippi Supreme Court. There, they made the precise arguments that FERC and the Court of Appeals rejected in the federal wholesale rate proceedings, stating that MP&L's "native load" is adequate, that Mississippi does not currently "need" any Grand Gulf 1 capacity and that, in any event, the 1974 Mississippi PSC certificate foreclosed any allocation of Grand Gulf 1 to MP&L until the mid-1990's.[20] MP&L responded that FERC had allocated the benefits and costs of all the capacity on the MSU System, including those of MP&L, and that FERC's determination of "just and reasonable" wholesale rates was binding on the Mississippi PSC under the Supremacy Clause and the Commerce Clause.

The Mississippi Supreme Court reversed, over Justice Robertson's dissent. It recognized that the FERC rate schedules and decisions required MP&L to begin incurring Grand Gulf 1 expenses on July 1, 1985. J.S. App. 11a. However, the Mississippi Supreme Court held that a Mississippi statute (*Miss. Code Ann.* § 77-3-39 (Supp. 1986)) required that the Grand Gulf 1 expenses be disallowed. This statute provides that the Mississippi PSC will determine the "reasonableness" of any "rate change," and disapprove any increase that is "unjust, unreasonable or unreasonably discriminatory." J.S. App. 70a-71a. The Mississippi

[19]*See* Edison Electric Institute, *Typical Residential, Commercial, and Industrial Bills, Investor-Owned Utilities, Winter 1987*, pp. 7-8, 35,45 (1987) (finding that the average MP&L customer with 1,000 kilowatt-hours of monthly usage has a bill of $70.66, whereas the national average is $73.79). MP&L's average residential customer uses about 1,000 kilowatt-hours a month.

[20]*Compare* Br. of Appellant State of Mississippi ex rel. Edwin Lloyd Pittman, Attorney General, pp. 1, 4-7, 15-16 (filed March 17, 1986), *with* pp. 11-13, *supra*.

Supreme Court interpreted this statute to require the Mississippi PSC to make its own determination of the "prudency" of MP&L's federally-mandated Grand Gulf 1 expenses *before* any of those costs could be included in retail revenue requirements and rates.[21] J.S. App. 13a-20a.

The Mississippi Supreme Court's Opinion concluded that "clearly the allocation of 33% of Grand Gulf power is unreasonably excessive" and that "the 1982 System Agreement providing for the allocation of 33% of its costs would seem to be imprudent." J.S. App. 15a-16a. It held that FERC has no right to "force[ ] unneeded power down the throats of Mississippi ratepayers." J.S. App. 15a. The basis for the Mississippi Supreme Court's conclusion that "Mississippi ratepayers simply do not need the energy generated by [Grand Gulf 1]" is that MP&L, as a "long" company, had "excess capacity" "before the Grand Gulf allocation" and that the average cost of Grand Gulf 1 electricity is almost four times that of MP&L's non-Grand Gulf 1 capacity. *E.g.*, J.S. App. 9a, 15a-16a.

The court also stated that "several aspects" of the prudence of Grand Gulf 1 were not decided by FERC and that the Mississippi PSC must decide these on the basis of *"local conditions"* before MP&L may recover any of this federally-prescribed expense. *Id.*, 17a-19a (emphasis in original). The Mississippi Supreme Court denied MP&L's timely petition for rehearing on May 20, 1987. *Id.*, 197a-198a.

[21]The Mississippi Supreme Court's opinion also refers to the Power Purchase Advance Payment Agreement under which MP&L and other MSU companies advanced MSE funds before the plant became operational, with the advance payments, plus interest, credited against future power payments. *See* J.S. App. 16a. These references are inexplicable because (1) MP&L's retail rates were not increased at all by reason of the advance payments (*see* J.S. App. 25a-59a), and (2) the advance payments have had no economic effect on MP&L because it has now received a full credit, plus interest.

On May 26, 1987, the Mississippi PSC took the action required by the Mississippi Supreme Court's mandate. It entered an order rescinding the September 16, 1985, rate increase and ordered MP&L to submit a plan for refunding the approximately $200 million in Grand Gulf 1 expenses that MP&L had collected since September 16, 1985. J.S. App. 199a-200a.

On June 1, 1987, and again on June 23, 1987, this Court entered orders staying the judgment of the Mississippi Supreme Court.[22] On October 5, 1987, this Court entered an order postponing consideration of jurisdiction over this appeal until the hearing on the merits. App. 23.

SUMMARY OF ARGUMENT

Appellate Jurisdiction. This Court has jurisdiction of this appeal under 28 U.S.C. § 1257(2). The constitutional validity of the lower court's application of *Miss. Code Ann.* § 77-3-39 was "drawn into question" in the Mississippi Supreme Court, and the court rejected MP&L's constitutional claims. *See Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 476 (1975); *Dahnke-Walker Milling Co.* v. *Bondurant*, 257 U.S. 282 (1921).

[22]On June 1, 1987, this Court stayed the judgment of the Mississippi Supreme Court "pending the timely filing and disposition of [this] appeal by this Court" and subject to "the posting of a good and sufficient bond, in manner and amount to be determined by the Supreme Court of Mississippi." 55 U.S.L.W. 3807.

While MP&L and its affiliates were obtaining the SEC regulatory approvals required to comply with the Mississippi Supreme Court's subsequent bonding order, the Mississippi PSC sought a temporary restraining order in Mississippi Chancery Court that would prohibit MP&L from recovering any Grand Gulf 1 expenses until an unconditional bond was posted. On June 19, 1987, the Mississippi Supreme Court summarily held, without giving MP&L an opportunity to respond, that this immediate "roll-back" was required by Mississippi law and had not been barred by this Court's June 1, 1987 stay. On June 23, 1987, this Court stayed the Mississippi Supreme Court's order of June 19, 1987. 56 U.S.L.W. 3001.

The necessary SEC approvals have now been obtained, and the required bonds have been filed with the Mississippi Supreme Court.

The Mississippi Supreme Court's decision is further a "final judgment" under at least two of the four recognized exceptions to the ordinary requirement of complete finality discussed in *Cox Broadcasting Corp., supra,* 420 U.S. at 477-87.

First, a state supreme court decision that finally resolves a major part of the case in a manner that threatens "irreparable harm" to a party is a "final judgment." *See Forgay* v. *Conrad,* 47 U.S. (6 How.) 201 (1848); *Radio Station WOW, Inc.* v. *Johnson,* 326 U.S. 120 (1945). Here, the Mississippi Supreme Court made a final determination that MP&L has no federal right to retain the over $200 million in Grand Gulf 1 expenses that it has collected since September, 1985. The order that these amounts be refunded and MP&L's rates immediately "rolled back" not only would irreparably harm MP&L, but also presents a federal question that "will survive and require decision regardless of the outcome of the future state [prudency] proceedings." *Cox Broadcasting Corp., supra,* 420 U.S. at 480.

Second, a state supreme court's rejection of a preemption challenge to state jurisdiction is "wholly separate and independent of the merits" of a dispute and a "final judgment." *Construction & General Laborers' Union* v. *Curry,* 371 U.S. 542, 548 (1963); *see Cox Broadcasting Corp., supra,* 420 U.S. at 483-84. Thus, this Court has recently exercised appellate jurisdiction over a case that raised the very Federal Power Act preemption claims presented by this case and that arose in the precise procedural posture of this case. *Nantahala Power & Light Co.* v. *Thornburg,* No. 85-1307, 106 S. Ct. 3268 (June 23, 1986) ("*Nantahala III*").

Federal Power Act Preemption. The decisions of this Court and state supreme courts uniformly reject the Mississippi Supreme Court's holding that states have jurisdiction to investigate the "prudence" of the power expenses that result from FERC-prescribed rate schedules and underlying interstate cost allocations. In *Nantahala Power & Light Co.* v. *Thornburg,* No. 85-568, 106 S. Ct. 2349 (June 17, 1986), the Court unequivocally

condemned a state's attempt to set retail rates on the premise that a local utility had acted "imprudently" in incurring the costs required by a FERC-filed rate. The Court held that, under the "filed rate doctrine," state utility commissions are required to do what the Mississippi Supreme Court has refused to do here: recognize the costs incurred under FERC rate schedules "as a reasonably incurred operating expense." Slip op. at 13; 106 S. Ct. at 2357. When a state believes that FERC rate schedules are unreasonable, its exclusive remedy is to exercise its rights under Sections 205 and 206 of the Federal Power Act and urge FERC to prescribe more favorable wholesale rates.

A contrary rule would defeat the central purpose of the Federal Power Act. It would allow individual states to burden interstate commerce by each individually seeking to impose cost allocations that advance their "respective local interests" at the expense of neighboring states. *See Public Utilities Commission* v. *Attleboro Steam & Electric Co.,* 273 U.S. 83, 89-90 (1927). The net result would be that integrated interstate power systems would be denied the ability to recover all the costs that were prudently incurred in meeting their customers demand and that the wholesale costs of local utilities would be "trapped." *Nantahala, supra,* slip op. at 16-17; 106 S. Ct. at 2359.

Litigation of these issues in each affected state would thus wholly defeat "the federal objective of providing orderly and streamlined procedures for approval of wholesale transactions." *Appeal of Sinclair Machine Products, Inc.,* 126 N.H. 822, 830, 498 A.2d 696, 702 (1985). It would further lead to the very "case-by-case" analysis of state action under the Commerce Clause that the Federal Power Act sought to avoid. *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Commission,* 461 U.S. 375, 380 (1983); *FPC* v. *Southern California Edison Co.,* 376 U.S. 205, 214-16 (1964).

The attempts to distinguish *Nantahala* are meritless. FERC made a determination of how all the low-cost and high-cost

power on the Middle South System should be allocated among the different states. The Mississippi Supreme Court's statement that MP&L does not "need" any of the high-cost Grand Gulf 1 power is simply a challenge to FERC's finding that MP&L should receive a 33% allocation of Grand Gulf 1, use correspondingly less low-cost capacity, and transfer the benefits of that low-cost capacity to other Middle South System companies.

Similarly, even assuming the decision in *Pike County Light & Power Co.* v. *Pennsylvania Public Utility Commission*, 77 Pa. Commw. 268, 273-74, 465 A.2d 735, 737-38 (1983), is correct, it is inapposite here for the same reason that it was in *Nantahala.* There, the Court rejected North Carolina's argument that under *Pike County*, Nantahala could be found to have been "imprudent" in purchasing such large quantities of high-cost TVA power on the ground that it should have obtained more of the low-cost hydroelectric and entitlements power. The Court reasoned that Nantahala "could not have treated itself as having access to any more low-cost entitlements power" than FERC had allocated to it. *Nantahala, supra,* slip op. at 19; 106 S. Ct. at 2360. The same principle governs here. FERC required MP&L to purchase 33% of the Grand Gulf 1 capacity. This means that MP&L uses correspondingly less of the low-cost capacity theoretically available to it. MP&L can no more be accused of imprudence in failing to acquire more low-cost power than could Nantahala.

The Mississippi Supreme Court is incorrect in asserting that there are "several aspects" of the "prudency" of Grand Gulf 1 that FERC has not decided and that state commissions may resolve. FERC found that Grand Gulf 1 was reasonably planned and reasonably completed to meet the demand of the Middle South System as a whole, so it determined the very prudence issues that Mississippi held to be open. More fundamentally, even if FERC had not made that determination, the exclusive means

by which a state may seek to disallow some of the costs of a facility used for interstate wholesale sales of electricity is to file a complaint with FERC under Sections 205 or 206 of the Federal Power Act. FERC was created precisely because it would burden commerce for individual states to make such determinations.

Commerce Clause. Finally, the Commerce Clause, by its own force, prohibits the state proceedings that the Mississippi Supreme Court has ordered. The Mississippi action is a stark example of the kind of state action that the Court generally invalidates "without further inquiry" (*Brown-Forman Distillers Corp.* v. *New York State Liquor Authority*, No. 84-2030, 106 S. Ct. 2080, 2084 (June 3, 1986)), and there is, in any event, no local interest that could justify this interference with Commerce Clause values.

Mississippi's conduct is indistinguishable from that which was at issue in *New England Power Co.* v. *New Hampshire*, 455 U.S. 331 (1982). The entire basis for Mississippi's claim that it does not "need" Grand Gulf 1 capacity is that there is enough "native" lower-cost capacity in Mississippi to serve MP&L's needs and that Mississippi should be able to reserve the economic benefits of this power for its citizens, rather than be required to use higher-cost Grand Gulf 1 power. This epitomizes the economic protectionism that is a *per se* violation of the Commerce Clause. Beyond that, Mississippi's assertion of jurisdiction has extra-territorial consequences; it would affect a plant that was reasonably planned and constructed to meet the needs of a four-state region. This in itself constitutes a severe burden on interstate commerce. *See Brown-Forman Distillers Corp., supra.*

In any event, there is no local interest that could justify this interference with interstate commerce. The decisive fact is that FERC already engages in plenary regulation of the matters that the Mississippi PSC would redetermine, and FERC's jurisdiction protects every legitimate interest that the state could assert. *See Edgar* v. *MITE Corp.*, 457 U.S. 624, 642 (1982). The only purpose that state review of the "prudency" of Grand Gulf 1 could

advance is the illegitimate one of protecting in-state economic interests at the expense of the interests of citizens in Louisiana, Arkansas, and Missouri.

ARGUMENT

This case presents the question of who is to determine how the costs of generating electricity are to be allocated among utilities that serve customers in different states and that obtain electricity from a single power pool: FERC under its explicit jurisdiction over these arrangements, or each of the affected states in the exercise of their separate jurisdiction over retail rates? This Court's decisions under the Federal Power Act and the Commerce Clause provide a very clear answer to this question. Indeed, the Court's recent decision in *Nantahala Power & Light Co. v. Thornburg*, No. 85-568, 106 S. Ct. 2349 (June 17, 1986), and its numerous precursors, establish that any state's jurisdiction to investigate the "prudency" of costs incurred under FERC rate schedules is preempted by the Federal Power Act. Under the filed rate doctrine, all such expenses must be treated as "a reasonably incurred operating expense." Slip op. at 13; 106 S. Ct. at 2357.

I. The Court Has Jurisdiction Over This Appeal Under 28 U.S.C. § 1257.

MP&L has invoked this Court's appellate jurisdiction under 28 U.S.C. § 1257(2).[23] By postponing the question of its jurisdiction, the Court has necessarily raised two questions: "(1) whether the constitutional validity of [a state statute] was 'drawn in question,' with the [Mississippi] Supreme Court upholding its validity, and (2) whether the decision from which this appeal has been taken is a '[f]inal judgment or decree.' " *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 476 (1975).

Appellate Jurisdiction. The Mississippi Supreme Court held that a state statute (*Miss. Code Ann.* § 77-3-39) requires the

[23] If that jurisdictional basis were held not to exist, 28 U.S.C. § 2103 requires that the appeal is to be treated as a petition for certiorari.

Mississippi PSC to determine MP&L's "prudency" in complying with the FERC rate schedules before any such costs may be recovered in MP&L's retail rates (J.S. App. 19a), and the Mississippi Supreme Court rejected MP&L's arguments that such a prudence review is preempted by the Federal Power Act and violates the Supremacy Clause and Commerce Clause. MP&L reiterated these arguments in its petition for rehearing, urging that this application of *Miss. Code Ann.* § 77-3-39 to Grand Gulf 1 expenses is unconstitutional. *See* MP&L's Petition for Rehearing, p. 2 (filed March 10, 1987). Because the constitutional validity of this statute as applied to these expenses was explicitly raised by MP&L in this fashion and decided by the state supreme court, the case is within the Court's appellate jurisdiction. *Cox Broadcasting Corp.*, *supra*, 420 U.S. at 476; *Dahnke-Walker Milling Co. v. Bondurant*, 257 U.S. 282, 290 (1921); *compare Richmond Newspapers, Inc. v. Virginia*, 448 U.S. 555, 562 n.4 (1980).

Final Judgment. Similarly, the fact that the Mississippi Supreme Court's decision anticipates "additional" Mississippi PSC proceedings to determine the "prudency" of MP&L's Grand Gulf 1 costs does not mean that the decision is not a "final judgment" under 28 U.S.C. § 1257.

The Mississippi Supreme Court finally rejected the federal claims that MP&L raised: that MP&L has had a federal right to recover in its retail rates all those expenses incurred since July 1, 1985, as Mississippi PSC's September 16, 1985 Final Order on Rehearing provided. The Mississippi Supreme Court held, in contrast, that MP&L may not recover any of these federally-mandated expenses unless and until the Mississippi PSC hereafter makes its own independent determination of MP&L's and Middle South's prudence. J.S. App. 19a. Thus, the Mississippi Supreme Court decision did not permit MP&L to continue to collect these expenses pending the future state commission decision. It required an immediate "roll-back" of MP&L rates to exclude the Grand Gulf 1 expenses and a refund of the some $200 million in

such expenses that has been collected since September, 1985—as ordered by the Mississippi PSC on May 26, 1987. *See* p. 21, *supra*. A further consequence of this order is that MP&L would have to write off the more than $431 million in Grand Gulf 1 deferred expenses as of May, 1987, which recovery was deferred under the Mississippi PSC's rate moderation plan. *See* p. 18, *supra*. As the Mississippi PSC found, MP&L "will quickly become insolvent" if it cannot collect its Grand Gulf 1 expenses and retain the amounts collected.[24]

It is because the Mississippi Supreme Court's decision has these immediate and irreparable consequences that this Court has entered two separate orders staying this state court judgment. *See* p. 21 & n. 22, *supra*. These same facts establish that the judgment is a final judgment under at least two of the four recognized exceptions to the ordinary requirement of complete finality that were discussed in *Cox Broadcasting Corp., supra*, 420 U.S. at 477-87.

First, it has been settled since *Forgay v. Conrad*, 47 U.S. (6 How.) 201 (1848), that a judgment that "resolve[s] a major part of the case in a manner that threatened irreparable harm to a party" is a "final judgment."[25] In *Forgay*, the Court held that a state court decision that finally rejected a federal claim and ordered the immediate transfer of property and money is a "final judgment," notwithstanding that additional state court proceedings (an accounting) had been ordered. 47 U.S. at 204.

[24]J.S. App. 29a. *See also* MP&L's Application for Stay of Final Judgment of the Supreme Court of Mississippi, pp. 14-19 (filed May 21, 1987).

[25]P. Bator, *et. al., Hart and Wechsler's Federal Courts and the Federal System*, p. 625 (2d ed. 1973); *see also* Note, The Finality Rule for Supreme Court Review of State Court Orders, 91 Harv. L. Rev. 1004, 1018 (1978). *Cf., Republic Natural Gas Co. v. Oklahoma*, 334 U.S. 62, 70 (1948) (finding no irreparable injury and no final judgment in case raising Due Process Clause challenge to a state interconnection order).

Accord Radio Station WOW, Inc. v. Johnson, 326 U.S. 120 (1945) (state court order requiring transfer of FCC radio license threatens "irremediable harm" and is a "final judgment"). The Court reasoned that if an interlocutory order requires a party "to deliver up property which he claims, or to pay money which he denies to be due, and the order immediately carried into execution," the party's "right of appeal is of very little value to him, and he may be ruined before he is permitted to avail himself of the right." 47 U.S. at 205. In *Forgay* and *Radio Station WOW*, the federal issue was "finally decided by the highest court in the State" and the issue of whether the transfer was required by federal law would "survive and require decision regardless of the outcome of future state [ ] proceedings." *Cox Broadcasting Corp., supra*, 420 U.S. at 480; *accord id.*, at 506 (Rehnquist, J., dissenting on other grounds).

These holdings are controlling here. The Court's earlier stay orders already establish that compliance with the Mississippi "transfer" orders (the roll-back and refund) will irreparably harm MP&L. Further, "short of settlement," nothing can occur in the further state commission proceedings that can "foreclose or make unnecessary" decision on MP&L's federal right to retain the more than $200 million in Grand Gulf 1 expenses that have been collected and the additional amounts that are collected each month. *See Cox Broadcasting Corp., supra*, 420 U.S. at 480. Even if the Mississippi PSC could hereafter conclude that all the Grand Gulf 1 expenses were prudently incurred—as it could not under the state supreme court's findings[26]—MP&L would, under the

[26]The Mississippi Supreme Court repeatedly stated that MP&L does not "need" any of the Grand Gulf 1 power and that it is imprudent for MP&L to have "purchased" such expensive power when MP&L has "excess capacity" without the Grand Gulf 1 allocation and when MP&L's native capacity is cheaper than Grand Gulf 1. *E.g.*, J.S. App. 9a, 16a. Thus, it would seem that the Mississippi Supreme Court has foreclosed a finding that any of MP&L's Grand Gulf 1 expenses were prudently incurred, and the Mississippi Supreme Court's decision is,
(Footnote continued on next page)

state court judgment, still only be entitled to recover those expenses prospectively, *i.e.*, from the date of the future state commission decision forward. Over $600 million in costs[27] would then still be "trapped," and the major part of the case unaffected. *Compare Nantahala, supra*, slip op. at 17-18; 106 S. Ct. at 2359.

Second, the Mississippi Supreme Court decision would be a final judgment even if the retroactive refund and roll-back orders had not been entered and even if the sole immediate consequence were to require litigation of the reasonableness of the Grand Gulf 1 expenses before the Mississippi PSC. This Court has repeatedly held that a state supreme court's rejection of a preemption challenge to state jurisdiction is "wholly separate from and independent of the merits" and a "final judgment." *Construction & General Laborers' Union v. Curry*, 371 U.S. 542, 548 (1963); *accord Merchantile National Bank v. Langdeau*, 371 U.S. 555 (1963) (rejection of claim that federal venue statute precludes state jurisdiction is final judgment); *see Cox Broadcasting Corp., supra*, 420 U.S. at 483-84.[28] This principal has special force here because the exercise of state jurisdiction over these prudence issues would itself create the very burdens on commerce that the Federal Power Act and the Commerce Clause were intended to prevent. *See* pp. 34-35, *infra*.

(Footnote continued from previous page)
therefore, a "final judgment" on the additional ground that MP&L cannot realistically "prevail" before the Mississippi PSC "on the facts or any nonfederal ground." *Cox Broadcasting Corp., supra*, 420 U.S. at 479; *see Construction & General Laborers' Union v. Curry*, 371 U.S. 542, 550-51 (1963); *Pope v. Atlantic C.L.R. Co.*, 345 U.S. 379, 382 (1953).

[27]As of May 1987, MP&L had $200 million in collections and $431 million in deferred expenses. *See* MP&L's Application for Stay of Final Judgment of Mississippi Supreme Court, pp. 14-19 (filed May 21, 1987).

[28]As the Chief Justice has stated, "where the proper forum for trying [an] issue" depends on resolution of a federal question, "sound judicial administration requires" that it be "decided by this Court . . . sooner rather than later." *Cox Broadcasting Corp., supra*, 420 U.S. at 506 (Rehnquist, J., dissenting on other grounds).

Thus, this Court recently applied this "exception" to exercise appellate jurisdiction over a state supreme court decision that rejected a Federal Power Act preemption claim in the precise procedural posture of this case. *Nantahala Power & Light Co. v. Thornburg*, No. 85-1307, 106 S. Ct. 3268 (June 23, 1986) ("*Nantahala III*").[29] These holdings are controlling here.

II. The Federal Power Act Preempts The Mississippi Statute As Applied To Grand Gulf 1.

The Mississippi Attorney General and the Mississippi Legal Services Coalition have challenged the "prudency" of MP&L's Grand Gulf 1 expense on a number of grounds. Each of these is simply a challenge to the manner in which FERC has allocated the benefits and costs of all the Middle South System's power (low-cost as well as high-cost) among MP&L and the other Middle South companies. The Mississippi Supreme Court's holding that a state statute requires the Mississippi PSC to make its own determination of the reasonableness of MP&L's FERC-mandated expenses is flatly contrary to the Federal Power Act and this Court's recent decision in *Nantahala*. If correct, states would have *carte blanche* to burden interstate commerce in precisely the ways Congress legislated to prevent. Indeed, here, the Mississippi Supreme Court stated that FERC's interstate

[29]In *Nantahala III*, as here, the state commission gave effect to the applicable FERC rate schedule in setting retail rates, but the North Carolina Supreme Court reversed on the ground that the state commission must itself investigate the reasonableness of the federally-prescribed costs. Nantahala appealed on the ground that the Federal Power Act barred the state commission from exercising jurisdiction over this issue. The question of the Court's appellate jurisdiction was fully briefed. *Nantahala Power & Light Co. v. North Carolina*, No. 85-1307, Jurisdictional Statement, pp. 5-6 (filed Feb. 3, 1986).

The Court did *not* dismiss the appeal for want of jurisdiction. Instead, it noted probable jurisdiction and remanded for reconsideration in light of *Nantahala I*. This holding would establish the Court's jurisdiction here even if there had been no immediate refund and roll-back order (as there was not in *Nantahala III*).

cost allocation is "unreasonably excessive" and "imprudent." J.S. App. 15a-16a.

A. The Federal Power Act Prevents States From Regulating Bulk Power Supply Arrangements.

The Federal Power Act was enacted because Congress, like this Court before it, recognized that the "uncontrolled regulation by the states" of the "production and transmission of energy" can "patently interfere with broader national interests."[30] Because these activities are "particularly likely to affect more than one State,"[31] state regulation would be an invitation to chaos. The reasonableness of the interstate wholesale transactions could be subject to litigation, and determinations, in multiple state commissions. Because all states would seek to advance "their respective local interests,"[32] the likely result would be both duplicative litigation and inconsistent state determinations that burden commerce.

Congress sought to prevent such interference with commerce by vesting the Federal Power Commission (now FERC) with exclusive jurisdiction to regulate the transmission and wholesale sales of electricity in interstate commerce. Congress drew "a bright line easily ascertained" to divide state and federal regulatory authority. *FPC v. Southern California Edison Co.*, *supra*, 376 U.S. at 215-16. Under this "bright line", states are prohibited from regulating these bulk power supply arrangements among affiliated as well as unaffiliated public utilities, regardless of the actual "impact of state regulation upon the national interest." *Id.*

[30] *Arkansas Elec. Coop. Corp. v. Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983). *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964); *Public Utils. Comm'n v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927).

[31] *Arkansas Elec. Coop. Corp.*, *supra*, 461 U.S. at 377.

[32] *Attleboro Steam & Electric Co.*, *supra*, 273 U.S. at 89-90.

At the same time, Congress directed FERC to resolve disputes over the interstate allocations of wholesale generation costs. Congress established an orderly, uniform procedure to make these and other wholesale rate determinations. Under Section 205 of the Act, every utility that provides electricity at wholesale in interstate commerce must file rate schedules showing all rates and charges, all classifications, practices, and regulations affecting such rates and charges, and all contracts affecting those rates and charges. 16 U.S.C. § 824d; J.S. App. 63a-67a. FERC is required to assure that these schedules and contracts affecting rates are "just, reasonable, and nondiscriminatory." *Id.*

Because wholesale rates become costs for purposes of the retail rates that states regulate, the Act further gives a significant role to states and state commissions. Section 306 provides that "[a]ny person, State, municipality, or State commission" may file complaints with FERC seeking modifications in the rate schedules under Sections 205 or 206 of the Act, and states may obtain judicial review of FERC decisions in federal courts of appeals. Federal Power Act, §§ 205, 206, 306; 16 U.S.C. §§ 824d, 824e(a), 825e; J.S. App. 63a-68a. There plainly would have been no need for these provisions if the federal remedies were not exclusive and if state commissions have jurisdiction to make their own determinations of the reasonableness of purchase power arrangements. *See Massachusetts Department of Public Utilities v. United States*, 729 F.2d 886, 888 (1st Cir. 1984).

Moreover, a state that investigated these arrangements would have irresistible incentives to adopt cost allocations that would advance its "respective local interests" and benefit "its residents to the detriment of its neighbors," or otherwise to disallow costs that FERC allocated to that state.[33] The result would be that the costs of local utilities would be "trapped"—because the utilities cannot pass through costs that they are required by FERC to

[33] *Attleboro Steam & Electric Co.*, *supra*, 273 U.S. at 89-90; *Massachusetts Dept. of Pub. Utils.*, *supra*, 729 F.2d at 888-89.

incur. An integrated system would thus be denied recovery of generation costs and investments that were prudently incurred to serve a multi-state area, but that appear "imprudent" to a state focusing only on local conditions. Those are the very burdens on commerce that Congress legislated to prevent.[34]

Beyond that, the mere assertion of state jurisdiction defeats the Congressional objective, regardless of how the state jurisdiction is exercised. Interstate rate and cost determinations would no longer be centralized in a single proceeding, and each of many affected states could relitigate the issues. As one state supreme court has held, "[s]uch a result defeats part of the federal objective of providing orderly and streamlined procedures for approval of wholesale transactions." *Appeal of Sinclair Machine Products, Inc.*, 126 N.H. 822, 830, 498 A.2d 696, 702 (1985).

Finally, if states had jurisdiction to determine these prudence issues under the Federal Power Act, it would have consequences other than permitting FERC's determinations to be relitigated, *ad infinitum*, in each of the affected states. The utilities whose costs are trapped would continue to have the right to challenge each state commission's reallocation of interstate wholesale costs in suits brought under the Commerce Clause—as they did before the Federal Act was passed. *See Attleboro Steam & Electric Co., supra*, 273 U.S. 83. While the Commerce Clause may be readily applied to invalidate the state action in the instant case (*see* pp. 43-45, *infra*), state rate orders arise in an "infinite variety of

[34]Because states would have unavoidable incentives to act in this way, this Court held in *Attleboro Steam & Electric Co., supra*, 273 U.S. at 89-90, that state regulation of interstate wholesale electric transaction is a *per se* violation of the Commerce Clause. By codifying this "bright line" in the Federal Power Act and declining to overrule *Attleboro* legislatively—as it could have, *Clark Distilling Co.* v. *Western Maryland Ry. Co.*, 242 U.S. 311 (1917); *Prudential Ins. Co.* v. *Benjamin*, 328 U.S. 408, 427-33 (1946)—Congress plainly intended to foreclose such interference with interstate wholesale sales of electricity.

cases." *Arkansas Electric Cooperative Corp., supra*, 461 U.S. at 390. One purpose of the Federal Power Act was to make "unnecessary" the very "case-by-case analys[e]s" under the Commerce Clause that Mississippi's position would require. *FPC* v. *Southern California Edison Co., supra*, 376 U.S. at 215-16. *See also Arkansas Electric Cooperative Corp., supra*, 461 U.S. at 380.

B. The Uniform Prior Holdings Of This Court And Of State Supreme Courts Prohibit State Jurisdiction Over Wholesale Electric Costs.

This Court's prior holdings bar any such state impairment of FERC's regulation. They establish that the Federal Power Act preempts any state law that can have the effect of "impair[ing] the Federal Commission's authority to regulate" wholesale sales in interstate commerce, either directly or indirectly. *Northern Natural Gas Co.* v. *State Corporation Commission*, 372 U.S. 84, 92 (1963).[35] State laws with far less direct consequences for FERC's regulation than Mississippi's have thus been held preempted.[36]

Most pertinent, the Court's "filed rate doctrine" protects FERC's exclusive jurisdiction by requiring that FERC-rate schedules be treated as lawful in any proceeding and by

[35]*See also Transcontinental Gas Pipe Line Corp.* v. *Mississippi State Oil & Gas Board*, No. 84-1076, 106 S. Ct. 709 (Jan. 22, 1986). While *Northern Natural Gas* and *Transcontinental Gas Pipe Line* were cases under the Natural Gas Act (15 U.S.C. §§ 717-717w) rather than the Federal Power Act, this Court has stated many times that the "relevant provisions of the two statutes 'are in all material respects substantially identical,'" and that it is the Court's "established practice" to "cit[e] interchangeably decisions interpreting the pertinent sections of the two statutes." *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 577 & n.7 (1981) (citations omitted).

[36]*See, e.g., Maryland* v. *Louisiana*, 451 U.S. 725, 749-50 (1981) (preempting a state tax statute on the ground it has the "effect" of "shifting the incidence of certain expenses" and "interfer[ed] with FERC's authority to regulate the proper determination of the allocation of costs.")

preempting any state law that would have the effect of "authoriz[ing] commerce in the commodity on other terms." *Montana-Dakota Utilities Co.* v. *Northwestern Public Service Co.*, 341 U.S. 246, 251 (1951). *See Arkansas Louisiana Gas Co., supra*, 453 U.S. at 578-80. The filed rate doctrine applies to all contracts affecting wholesale rates that FERC regulates. *Nantahala, supra*, slip op. at 8-13; 106 S. Ct. at 2354-57.

Nantahala is indistinguishable from this case. There, a North Carolina utility (Nantahala) entered into contracts under which it and an affiliated utility serving Tennessee (Tapoco) pooled their low-cost hydroelectric power and transferred it to the Tennessee Valley Authority ("TVA"). In exchange, each utility received fixed annual "entitlements" of TVA power and the right to purchase high-cost TVA power to the extent each's entitlements were insufficient. There, as here, extensive wholesale proceedings occurred before FERC to determine the reasonableness of these arrangements and of the interstate allocations of the low-cost entitlement and the high-cost purchased power. There, as here, North Carolina urged FERC to nullify the contracts or otherwise to order an allocation of the low-cost power that was far more favorable to retail ratepayers in North Carolina. When that effort was unsuccessful, North Carolina attempted to use its retail ratemaking authority to nullify FERC's decisions by setting retail rates as if a radically different interstate allocation had been ordered.

This Court unanimously reversed the North Carolina retail rate order, unequivocally condemning this state interference with FERC's exclusive jurisdiction (slip op. at 13; 106 S. Ct. at 2357):

> "Once FERC sets such a rate, a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A state must rather give effect to Congress's desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority."

Specifically, *Nantahala* held that the rate schedules "filed with FERC or fixed by FERC must be given binding effect by state utility commissions determining intrastate rates" (slip op. at 8; 106 S. Ct. at 2354), and that the costs incurred under these rate schedules must be treated "as a reasonably incurred operating expense for the purpose of setting an appropriate retail rate." Slip op. at 13; 106 S. Ct. at 2357. Otherwise, the Court held that "Nantahala cannot fully recover its costs of purchasing at the FERC-approved rate" and "[a] portion of [those FERC-prescribed] costs" would be "therefore 'trapped.' " Slip op. at 17; 106 S. Ct. at 2359.

In so holding, *Nantahala* merely followed the decisions of numerous state supreme courts that have recognized these very principles in cases indistinguishable from the case at bar.[37] For example, in *Nantahala*, the Court relied (slip op. at 11-12; 106 S. Ct. at 2356) upon the decision of the Massachusetts Supreme Judicial Court in *Eastern Edison Co.* v. *Massachusetts Department of Public Utilities*, 388 Mass. 292, 446 N.E.2d 684 (1983). There, Eastern Edison acquired power from an affiliate under the FERC rate schedule that recouped the investment in an abandoned nuclear plant. As here, the claim was made that this investment was not "needed" by Massachusetts ratepayers—and

[37]*See, e.g.*, *Narragansett Electric Co.* v. *Burke*, 119 R.I. 559, 381 A.2d 1358 (1977) *cert. denied*, 435 U.S. 972 (1978); *Northern States Power Co.* v. *Minnesota Public Utilities Commission*, 344 N.W.2d 374 (Minn.), *cert. denied*, 467 U.S. 1256 (1984); *Northern States Power Co.* v. *Hagen*, 314 N.W.2d 32 (N.D. 1981); *Public Serv. Co. of Colorado* v. *Public Utils. Comm'n*, 644 P.2d 933, 939 (Colo. 1982); *Washington Gas Light Co.* v. *Public Serv. Comm'n*, 452 A.2d 375 (D.C. App. 1982), *cert. denied*, 462 U.S. 1107 (1983); *United Gas Corp.* v. *Mississippi Pub. Serv. Comm'n*, 240 Miss. 405, 127 So. 2d 404 (1961); *Natural Gas Pipeline Co. of America* v. *Illinois Commerce Comm'n*, 33 Ill. 2d 214, 222, 210 N.E.2d 490, 494 (1965).

A federal court of appeals has followed these decisions in a case involving the very interstate wholesale rates and cost allocations at issue here. *Arkansas Power & Light Co.* v. *Missouri Public Service Comm'n*, 829 F.2d 1444, 1451-52 (8th Cir. 1987); *see also Appalachian Power Co.* v. *Public Service Comm'n of West Virginia*, 812 F.2d 898 (4th Cir. 1987).

clearly it was not because the plant was abandoned. Nevertheless, the Massachusetts court held that FERC alone has jurisdiction to determine the prudence of this investment and that all Edison Electric's purchased power expenses under this FERC filed rate must be treated as reasonable operating expenses, and included in retail rates unless and until FERC prescribes a different filed rate. 446 N.E. 2d at 687.

These decisions recognize that a state commission's exclusive means of protecting the interests of retail ratepayers is to do what the Mississippi PSC did here: intervene in the FERC proceedings to urge lower wholesale rates and make provisions in its retail rate order for reductions or refunds to the extent FERC later so orders. *See Narragansett Electric Co., supra*, 119 R.I. at 568, 381 A.2d at 1363; p. 18 n. 18, *supra*. As stated in another state court decision cited in *Nantahala* (*see* slip op. at 11-12, 14; 106 S. Ct. at 2356-57), state commissions have no jurisdiction to inquire into the reasonableness or prudence of expenses incurred under FERC rate schedules; this "jurisdiction . . . rests exclusively with FERC." *Public Service Co. of Colorado* v. *Public Utilities Commission*, 644 P.2d 933, 940 (Colo. 1982). In contrast, the Mississippi Supreme Court here stated that MP&L's federally-prescribed Grand Gulf 1 expenses are "unreasonably excessive" and appear to be "imprudent." J.S. App. 15a-16a.

C. The Attempts To Distinguish *Nantahala* Are Meritless.

Nantahala and its numerous precursors control this case. The Federal Power Act deprives the Mississippi PSC of any jurisdiction to investigate the prudence of MP&L's Grand Gulf 1 expenses and requires that these costs be treated as a "reasonably incurred operating expense" and included in MP&L's retail rates. *Nantahala, supra*, slip op. at 13; 106 S. Ct. at 2357. Otherwise, MP&L would be required to incur some $25 million in monthly Grand Gulf 1 expenses by FERC, prohibited from recovering those same costs from its customers, and left with millions of

dollars of "trapped costs," contrary to *Nantahala*'s explicit holding. Slip op. at 18; 106 S. Ct. at 2359.

The Mississippi Supreme Court attempts to distinguish *Nantahala* on three different grounds. Each underscores the impermissible interference with FERC's jurisdiction.

First, the Mississippi Supreme Court stated that *Nantahala* does not require a state commission to set rates "based on the construction and operation of a plant (nuclear or otherwise) that generates power that is not needed at a price that is not prudent." J.S. App. 15a. This is a direct challenge both to FERC's jurisdiction over this issue and to its explicit contrary findings.

The entire basis for the assertion that MP&L does not "need" Grand Gulf 1 capacity is the Mississippi Supreme Court's finding that MP&L has enough lower-cost "native" capacity to meet the needs of Mississippi ratepayers, and that this lower-cost capacity would be sufficient into the 1990s. *See* J.S. App. 9a, 15a-16a. Similarly, in *Nantahala*, North Carolina asserted that Nantahala did not need TVA purchased power because it had title to adequate hydroelectric facilities. The decisive fact here is that FERC found that MP&L's capacity was acquired to serve the Middle South System as a whole, not just Mississippi (*see* pp. 11-15, *supra*), and that it is "just and reasonable" for MP&L to be allocated 33% of the higher-cost Grand Gulf 1 capacity and to receive the benefits of correspondingly less of the low-cost power. *See id.*

In so holding, FERC found that these allocations would roughly equalize generation costs among the MSU companies. FERC specifically rejected the Mississippi arguments that MP&L's acquisition of this low-cost capacity should give MP&L dramatically lower costs and excuse Mississippi from paying for higher-cost capacity that FERC found was also reasonably acquired to meet the needs of the Middle South System as a whole. *See* pp. 11-13, *supra*. Thus, FERC held that the

Mississippi position is "unjust, unreasonable, and discriminatory," and this finding was unanimously affirmed by the Court of Appeals (with no party having sought Supreme Court review of this finding). See pp. 11-13, *supra*.

Second, the Mississippi Supreme Court relies on the fact that the Court's decision in *Nantahala* assumed, without deciding, that the decisions in cases such as *Pike County Light & Power Co. v. Pennsylvania Public Utility Commission*, 77 Pa. Commw. 268, 273-74, 465 A.2d 735, 737-38 (1983), and *Appeal of Sinclair Machine Products, Inc.*, 126 N.H. 822, 498 A.2d 696 (1985), are consistent with the Federal Power Act. *See* J.S. App. 15a-17a. In each, FERC had, in the state court's view, merely approved the wholesale utility's price terms, but had not determined whether it was reasonable for a retail utility to have purchased "a particular *quantity* of power [at that price when] lower-cost power is available elsewhere." *Nantahala, supra*, slip op. at 19; 106 S. Ct. at 2360 (emphasis in original). The state courts reasoned that they were resolving "matters not resolved by the FERC" either "expressly or impliedly." *Appeal of Sinclair Machine Products, Inc., supra*, 126 N.H. at 833, 498 A.2d at 704.

The *Pike County* line of decisions is inapposite here for the same reason that it was in *Nantahala*: FERC here determined the "quantity" of the high-cost and low-cost power that MP&L would obtain. In *Nantahala*, North Carolina had contended that it had been imprudent for Nantahala to purchase large quantities of high-cost power from TVA because it should have obtained more of the low-cost entitlements power. The Court rejected that argument. It held that "Nantahala's procurement of [TVA] purchased power" could not be held to be "unreasonably large" because the FERC rate schedules allocated the high-cost and low-cost power. Thus, Nantahala "could not have treated itself as having access to any more low-cost entitlement power than it is eligible to include under FERC's interpretation of what would be a fair allocation." *Nantahala, supra*, slip op. at 19; 106 S. Ct. at 2360.

The same principle governs here. FERC had all the power sources in the Middle South System before it: low cost as well as high cost. FERC allocated MP&L 33% of the Grand Gulf 1 capacity, and denied it the benefits of corresponding amounts of the lower cost capacity on the system. Indeed, FERC ordered greater purchases of capacity than individual companies had agreed to,[38] and increased MP&L's Grand Gulf 1 allocation to 33% in the face of its own argument that a lower allocation should be ordered. *See* p. 13, *supra*. This makes it explicit that individual MSU companies have no individual discretion in these matters, and that MP&L can no more be accused of imprudence in failing to obtain more low-cost and less high-cost power than could Nantahala.[39] As in *Nantahala*, therefore, this Court may assume, without deciding, that *Pike County* is consistent with the Federal Power Act.

Finally, the Mississippi Supreme Court seeks to distinguish *Nantahala* by arguing that there are "several aspects" of MP&L's "prudency" that were not at issue in the FERC proceedings and that state authorities are free to make these determinations. Specifically, the court stated that "we have yet to see MP&L, [MSE], or MSU justify putting Grand Gulf on line at its exorbitant cost" and that FERC "was never presented with the question of whether the completion of Grand Gulf, or its continued operation, was prudent." J.S. App. 17a. These claims are mistaken for two reasons.

Foremost, FERC's jurisdiction to establish the "just and reasonable" rates under which MP&L and other Middle South operating companies acquire Grand Gulf 1 power from MSE, *a*

[38]For example, FERC ordered AP&L to purchase 36% of the Grand Gulf 1 when AP&L had not agreed to pay for *any* of that power in the UPSA. *See* p. 15, *supra*.

[39]This is especially so because MSU is a public utility holding company and the MSU System is required to operate as a single interconnected system, under power pooling agreements regulated by FERC. *See* pp. 4-5, *supra*.

fortiori, includes the jurisdiction to determine whether any of the underlying costs and investment of the utility (MSE) were imprudently incurred, and must therefore be excluded from MSE's wholesale rates.[40] In the FERC proceedings, MSE introduced evidence to prove, and FERC expressly found, that Grand Gulf 1 was reasonably planned and completed by the Middle South System to meet demand in the system as a whole, and no party appealed that finding. *See* pp. 13-14 n.13, *supra*. FERC has thus permitted MSE to earn a return on 100% of its Grand Gulf 1 investment in the wholesale rates it has charged MP&L and other Middle South companies since July 1, 1985.

More fundamentally, even if FERC had not made findings and the issue were still open, the exclusive means by which a state may seek to disallow some of this investment on prudence grounds is to file a complaint with FERC under Sections 205 or 206 of the Federal Power Act. The reasonableness or prudence of a utility's investment is central to FERC's core authority to determine just and reasonable rates. A state may not assume this jurisdiction by declining to litigate prudence before FERC.

This is especially so because the "prudency" of a multi-state project like Grand Gulf 1 that was built to meet the needs of a four-state system "as a whole" is beyond the institutional competence of a single state to assess. If the Mississippi Supreme Court were correct that states may make this determination "*in light of local conditions*" and the "needs" of individual companies (J.S. App. 18a-19a) (emphasis in original), it would subvert the Act. FERC was created precisely because the "prudency" of wholesale investments in plants planned and built to sell power in interstate commerce to different local utilities should

[40] As the Fourth Circuit has held, a FERC finding that a wholesale cost allocation and rates are "just and reasonable" is a determination of "prudence." *Appalachian Power Co.*, *supra*, 812 F.2d at 903-04. Indeed, the Mississippi Supreme Court held in this case that a statutory directive to assure that rates are "just and reasonable" necessarily encompasses determining whether underlying costs were "prudent." J.S. App. 13a.

be determined by a federal agency that will assess regional and national needs, not purely local ones. *See Arkansas Electric Cooperative Corp.*, *supra*, 461 U.S. at 377; *FPC* v. *Southern California Edison Co.*, 376 U.S. 205 (1964). As the Court recognized in *Pacific Gas & Electric Co.* v. *State Energy Resources Conservation & Development Commission*, 461 U.S. 190, 205 (1983), FERC has "broad authority . . . over the need for and pricing of electrical power transmitted in interstate commerce."

III. The Application Of The Mississippi Statute Violates The Commerce Clause.

Finally, even if the Federal Power Act did not preempt Mississippi's actions, the Commerce Clause, by its own force, would prohibit the state proceedings that the Mississippi Supreme Court has ordered. Indeed, the Eighth Circuit has held that the Commerce Clause prohibits a state from investigating the interstate wholesale rates and cost allocations that are at issue in this case and enjoined such state proceedings on this ground. *Middle South Energy, Inc.* v. *Arkansas Public Service Commission*, 772 F.2d 404 (8th Cir. 1985), *cert. denied*, 474 U.S. 1102 (1986).

This Court has adopted a two-level inquiry in analyzing state economic regulations under the Commerce Clause. When the application of a state statute has the purpose or effect of favoring in-state economic interests over out-of-state interests or directly regulates out-of-state economic interests, the Court has "generally struck down the statute without further inquiry." *Brown-Forman Distillers Corp.* v. *New York State Liquor Authority*, No. 84-2030, 106 S. Ct. 2080, 2084 (June 3, 1986); *see New England Power Co.* v. *New Hampshire*, 455 U.S. 331 (1982); *Philadelphia* v. *New Jersey*, 437 U.S. 617 (1978). Other economic regulation will be invalidated only if the burden on interstate commerce exceeds the benefits the state derives from the statute. *Pike* v. *Bruce Church, Inc.*, 397 U.S. 137 (1970). The Mississippi Su-

preme Court's application of *Miss. Code Ann.* § 77-3-39 is unconstitutional under both tests.

A. Mississippi's Proposed Actions Are *Per Se* Invalid.

First, it is apparent from the face of the Mississippi Supreme Court opinion that it is a stark, clear example of the "most serious concern [under the Commerce Clause]—economic protectionism." *Arkansas Electric Cooperative Corp., supra*, 461 U.S. at 394. The basis for Mississippi's challenge to the "prudency" of FERC's allocation of 33% of Grand Gulf 1 capacity to MP&L is that MP&L owns enough "native" capacity in Mississippi to serve the needs of MP&L's customers. It asserts that MP&L should not be effectively required to transfer those benefits to other Middle South states under the FERC rate schedules, and ordered to use the higher-cost Grand Gulf 1 capacity instead. *See* J.A. App. 15a; p. 11 n.12 & p. 17 n.16, *supra*.

This conduct is indistinguishable from that at issue in *New England Power Co.* v. *New Hampshire, supra*. There, the state of New Hampshire attempted to preserve for its citizens the exclusive economic benefits of the low-cost hydroelectric power generated in that state. 455 U.S. at 336, 343-44 n.10. The Court held that for New Hampshire even to attempt to force such reallocations of power supply costs was a *per se* violation of the Commerce Clause, and this attempt must be enjoined before it had any adverse consequences.

Moreover, Mississippi's actions would have extra-territorial consequences. Indeed, it is asserting the authority to adjudge that a generating facility that was planned and constructed to serve customers throughout a four-state area should not have been built at all and to enter coercive orders on that basis, despite the fact that the plant is now meeting demand in the Middle South region. Any steps that the Mississippi PSC takes to prevent MP&L from recovering its Grand Gulf 1 payments of this facility would jeopardize MSE's revenues and thus impair the operation of a plant that makes wholesale sales in interstate commerce in a four-state area. That would represent a "direct restraint on interstate commerce" with the kind of "extraterritorial effect" that has been held to be a *per se* violation of the Commerce Clause. *Edgar* v. *MITE Corp.*, 457 U.S. 624, 642 (1982); *cf.*, *Arkansas Electric Cooperative Corp.*, *supra*, 461 U.S. at 377-79.

B. There Are No Local Benefits That Can Justify This Burden On Commerce.

In any event, the Mississippi actions cannot survive a balancing test under *Pike* v. *Bruce Church*, *supra*. For the reasons stated above, the burden upon, and interference with, the values protected by the Commerce Clause is stark. Conversely, there is no local interest that could possibly justify these burdens.

The sufficiency of a state's interest must be assessed against the background of the protections and safeguards that federal law already provides. *Edgar* v. *MITE Corp., supra*, 457 U.S. at 644-45. *See Arkansas Electric Cooperative Corp.*, *supra*, 461 U.S. at 393 (emphasizing that absence of federal regulation was critical to holding in that case). Here, FERC engages in plenary regulation of wholesale transfers of electricity to protect the very interests that Mississippi asserts, with FERC having jurisdiction to disallow any investment or expenditures that were imprudently made as well as having authority to assure that cost allocations are just, reasonable, and nondiscriminatory. Conversely, Mississippi has no legitimate interest in regulating to "go beyond" FERC. *Edgar* v. *MITE Corp.*, *supra*, 457 U.S. at 644-45. Under the circumstance, the only purpose that state review of the "prudency" of Grand Gulf could advance is an illegitimate one: to relitigate the very issues FERC decided in order to protect in-state economic interests at the expense of the interests of citizens in Louisiana, Arkansas, and Missouri. All Mississippi's legitimate interests are being fully protected by FERC.

CONCLUSION

For the reasons stated, the judgment of the Mississippi Supreme Court should be reversed.

Respectfully submitted,

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi 39205
(601) 354-2385

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 298-1800

Of Counsel:

WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

Attorneys for Appellant

Dated: December 3, 1987

* *Counsel of Record*

APPELLEE'S

BRIEF

TABLE OF CONTENTS

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

No. 86-1970

In The

Supreme Court of the United States

October Term, 1987

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN, Attorney General, and THE MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF FOR APPELLEE

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

All Constitutional provisions and statutes cited by the Appellee have previously been set forth in Appellant's Jurisdictional Statement, in Appellee's Motion to Dismiss, or in the Joint Appendix.

I. STATEMENT OF THE CASE

This case involves an appeal of a decision of the Mississippi Supreme Court issued on February 25, 1987, reversing an Order of the Mississippi Public Service Commission ("MPSC"). *State of Mississippi, ex rel. Edwin*

Lloyd Pittman, Attorney General, et al. v. Mississippi Public Service Commission, et al., No. 56,762 (Miss. Supreme Court, February, 1987) (One Justice Dissenting) which granted Mississippi Power & Light Company ("MP&L") a $326,547,000 rate increase based on a 33% cost allocation of the Grand Gulf Nuclear Plant as approved by the Federal Energy Regulatory Commission ("FERC"). The MPSC Order was reversed by the Supreme Court of Mississippi for its failure to comply with its statutory mandate (*Miss. Code Ann.* § 77-3-39 (1986 Supp.)) to review the prudency of investment before enacting retail rates based on its cost.

> "We do not interpret the law to require that we approve the blind pass-through of a $326 million rate increase to Mississippians without a prudency review; to do so would be a gross abdication of the responsibility of State regulators." *State of Mississippi v. Miss. Public Service Commission.* (Appendix 14a.)

In the interest of brevity, Mississippi Legal Services Coalition ("MLSC") adopts by reference the "Background" section of the Supreme Court of Mississippi Decision (App. 3a-13a) as its Statement of the Case through the proceedings of the Federal Energy Regulatory Commission ("FERC") and the Mississippi Public Service Commission ("MPSC"). In addition, MLSC states as follows:

MLSC represents low-income and elderly ratepayers in the 44 counties served by MP&L. Some of these counties are the poorest in the United States, according to the 1980 Census of Population, U.S. Department of Commerce, Bureau of the Census, General Social and Economic Characteristics. The 1980 per capital income was $5,183.00, and the percent of persons below the poverty level was 23.9%. (Table 57, p. 26-14)

By statute, the Mississippi Public Service Commission is to enter rates that are balanced and that provide a fair return to the utility at a fair and reasonable rate to the consumer. *See, e.g.*, the Public Utility Act of 1956, 1956 Mississippi Laws, Chapter 372; § 77-3-33, *Miss. Code Ann.* (1986 Supp.).

The allowance of a blind pass-through of such a large wholesale cost to the retail ratepayers without a prudency determination will have a severe and irrevocable impact on the low-income and elderly consumer ratepayers of MP&L. A reversal of the Mississippi Supreme Court decision would leave these customers in a posture of continuing to pay high utility rates which have never been properly determined to be just and reasonable.

The Mississippi Supreme Court specifically recognized the FERC's wholesale rate allocation of Grand Gulf I costs and did not seek to abolish the rate or to have MP&L pay a rate other than that mandated by the FERC. The overruling of the Mississippi Supreme Court Order will cause state utility regulatory commissions to dispute their traditional role of determining just and reasonable rates.

SUMMARY OF ARGUMENT

Mississippi Legal Services Coalition (MLSC) seeks an affirmance of the Supreme Court of Mississippi decision

requiring the Mississippi Public Service Commission (MPSC) to conduct a prudency hearing to determine just and reasonable rates prior to a "blind pass-through" of a 327 million dollar retail rate increase.

The Mississippi Supreme Court's decision was drawn to effectuate no interference of the Federal Regulatory Scheme of the FERC's jurisdiction to set interstate wholesale rates.

> "We are aware of the effect that wholesale rates have on retail rates, and we do not challenge the FERC's jurisdiction over interstate wholesale rates." *State of Mississippi, ex rel., Edwin Lloyd Pittman, et al. v. Mississippi Public Service Commisson, et al.*, No. 56,762 (Feb. 27, 1987) at p. 15.

The Order of a State Utility Regulatory Commission conducting a prudency review to determine what cost should be reflected in local retail rates lies exclusively with the State agency. *Nantahala Power & Light Co. v. Thornburg,* 106 S.Ct. at 2357-58.

Notwithstanding Appellants' assertions to the contrary, the application of the Supreme Court of Mississippi Order does not violate the Commerce Clause. The Court's decision regulates evenhandedly, and does not constitute an impermissible burden on interstate commerce. The Order does not prohibit the exportation of energy out of the State, and any effects on interstate commerce are merely incidental and are outweighed by the State interest in providing reasonable retail rates to its consumers. *Pike v. Bruce Church,* 397 U.S. 137, 25 L.Ed.2d 174, 90 S.Ct. 844 (1970).

—o—

ARGUMENT

I. STATE REGULATORY COMMISSION'S JURISDICTION TO CONDUCT PRUDENCY REVIEW TO DETERMINE WHAT COST SHOULD BE REFLECTED IN RETAIL RATES IS NOT PREEMPTED BY THE FEDERAL POWER ACT.

MP&L, the Solicitor-General and Edison Electric in an amicus curiae brief, have advanced the argument in their briefs that Congress, through the enactment of the Federal Power Act, has preempted State jurisdiction to review the prudency of an investment such as Grand Gulf before it can adopt retail rates based on its cost. We disagree.

In Part II of the Federal Power Act, 16 U.S.C. §§ 824-824k, Congress in 1935 "delegated to the Federal Power Commission, now the Federal Energy Regulatory Commission [FERC] exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce, without regard to the source of production." *New England Power Co. v. New Hampshire,* 455 U.S. 331, 340 (1982). This 1935 enactment was a "direct result" of the Supreme Court's holding in *Public Utilities Commission v. Attleboro Steam and Electric Company,* 273 U.S. 83 (1927), "that the states lacked power to regulate the rates governing interstate sales of electricity for resale." *New England Power Co.,* 455 U.S. at 340. The Federal Power Act, however, explicitly denied the FERC's jurisdiction "over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce." 16 U.S.C. § 824(b)(1). Congress created a "bright line" between federal and state jurisdiction, deny-

ing "state power to regulate a sale 'at wholesale to local distributing companies' and allow[ing] state regulation of the sale 'at local retail rates to ultimate consumers.'" *F.P.C. v. Southern California Edison Co.*, 376 U.S. 205, 214 (1964) (quoting *Illinois Natural Gas Co. v. Central Illinois Public Service Co.*, 314 U.S. 498, 504 (1942)). *Cf. Louisiana Public Service Comm. v. F.C.C.*, 106 S.Ct. 1890 (1986) (discussing dual system of state and federal regulation over telephone service embodied by Communications Act of 1934; concluding that Act did not preempt state regulation over depreciation of dual jurisdiction property for intrastate ratemaking purposes).

The existence of this "bright line" affects the way Appellants view a preemption claim involving the Federal Power Act. MP&L has endeavored to describe the circumstances before this Court as one in which the Mississippi Supreme Court's decision is stepping into the field of wholesale rate making, an area under the exclusive jurisdiction of FERC. MP&L alleges that the Mississippi Supreme Court decision disrupts the Federal Scheme. However, a reversal of the Mississippi Supreme Court Order would cause an improper expansion of the FERC jurisdiction and directly intrude on the State Regulatory Scheme to set just and reasonable retail rates.

While the Supreme Court in *Nantahala Power & Light Co. v. Thornburg*, 106 S.Ct. 2349 (1986), required that the North Carolina Utility Commission recognize the FERC-determined wholesale costs, the court also recognized that retail rates need not necessarily be increased to reflect the corresponding increase in wholesale rates set by the FERC. State Commissions are permitted by the Federal

Power Act to treat a proposed rate increase as any other filing, and review the Company's entire financial structure to determine whether or not savings exist in other areas relevant to the setting of retail rates, 106 S.Ct. at 2357-58.

MLSC maintains that the Mississippi Supreme Court's decision merely regulates the extent to which MP&L may pass its wholesale cost through to consumers in its retail rates. The Court determined that the extent to which wholesale costs should be reflected in local utility rates lies exclusively with the state agency. *Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), *cert. den.*, 435 U.S. 972 (1978).

In the *Narragansett* case, a Rhode Island utility attempted to pass through to its retail customers the increased cost of electric power purchased from its wholesale supplier. The utility filed with the Public Utility Commission (PUC) a notice of price adjustment pursuant to the PUC's purchased power cost adjustment (PPCA) regulations. The PUC ruled that although it could not regulate the wholesale rate, which was within the exclusive jurisdiction of the FPC, it could nevertheless investigate the reasonableness of the costs underlying the wholesale rate. The PUC therefore determined that it would prohibit the utility from passing through to its retail customers any portion of the wholesale costs that were "strikingly" or "glaringly" unreasonable.

On appeal, the Rhode Island Supreme Court held that it was improper for the PUC to investigate the reasonableness of the utility's FPC-approved wholesale costs, and that it must treat those costs as reasonable operating ex-

penses. Under the state's PPCA regulations, however, the PUC was not required to adjust the utility's retail rates automatically to reflect the higher wholesale costs. Rather, the PUC was entitled to "treat the proposed rate increase as it treats other filings for charged rates under [a state statute] and investigate the overall financial structure of [the utility] to determine whether the company has experienced savings in other areas which might offset the increased price for power." 119 R.I. at 568, 381 A.2d at 1363.

On remand, the MPSC may determine, after a prudency review, that savings exist in a number of other areas that could be used to lessen the impact of the large wholesale rate increase on the retail ratepayers.

A decision of a state appellate court considering this issue reached a similar conclusion in the application of the *doctrine of preemption.* In *Pike County Light & Power Company v. Pennsylvania Public Utility Commission,* 77 Pa.Commw. 268, 465 A.2d 735 (Pa. 1983), FERC had approved an [agreement for the purchase by a utility from its parent of wholesale power.] In setting the utility's retail rates, the Commission held that although it could not challenge the rates as being unreasonable, it could disallow purchase power expenses on the ground that more economical sources of supply were available.

The utility appealed the ruling, arguing that the PUC was preempted from disallowing part of its FERC-approved wholesale costs to be passed through to its retail ratepayers. The court disagreed:

> "The FERC forcuses on Orange & Rockland [the wholesale supplier] to determine whether it is just and reasonable *for that company to charge* a particular rate, but makes no determination of whether it is just and reasonable *for Pike* [the utility] *to incur* such a rate as an expense. The PUC, on the other hand, has no jurisdiction to analyze Orange & Rockland's cost of service data and makes no determination as to the reasonableness for Orange & Rockland to charge its rates. The PUC focuses on Pike and its cost of service data to determine whether it is reasonable for Pike to incur such costs in light of available alternatives. So while the FERC determines whether it is against the public interest for Orange & Rockland to charge a particular rate in light of its costs, the PUC determines whether it is against the public interest for Pike to pay a particular price in light of its alternatives." (465 A.2d at 738)

The Court held that the regulatory functions of the FERC and State Commissions do not encroach on the Federal Power Act and expressly preserves the Public Utility's authority to determine the reasonableness of the Utility's claimed expense.

In *Commonwealth Electric Co. v. Department of Public Utilities,* 397 Mass. 361, 491 N.E.2d 1035 (1986), retail utility applied for approval for change in allowed fuel charge due to increased cost of purchasing wholesale electricity following power outage at utility's contractual supplier. On appeal, the utility argued that because the rates it must pay to its wholesale suppliers are fixed by the FERC regulation, oversight of these rates by DPU frustrates the purposes of the FPA. The Supreme Judicial Court disagreed and held that:

> ". . . while the DPU cannot inquire into the reasonableness of wholesale rates fixed by FERC. *Eastern Edison, supra,* the DPU may inquire whether a purchaser, such as the company, is warranted in agree-

ing to purchase at such a rate considering its alternatives. *Appeal of Sinclair Mach. Prods., Inc.*, 126 N.H. 822, 498 A.2d 696, 699 (1985)."

Therefore, under the Federal Power Act, 16 U.S.C. § 824(a), Congress created a complementary regulatory framework wherein the states lost no authority as a result of the Act and the federal role filled the gap in state regulation which had been created by the *Attleboro* case. FERC's jruisdiction does not negate the jurisdiction of the states over the same facilities to, *inter alia*, approve their construction, establish and allocate their value in rate base, evaluate their operation and maintenance expenses and establish retail rates to recover reasonably incurred costs, access their books and records. Quite simply, a dual regulatory system was created by Congress in 1935 and has existed for over fifty years. The FERC was given the authority to set wholesale rates for interstate sale and transmission of electricity, but otherwise the power of the states was unaffected. A review of the exemption contained in the Federal Power Act is very specific, as is shown in the relevant clause:

> *Federal Power Act*, 16 U.S.C. § 824(a)—"It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest and that Federal regulation of . . . that part of such business which consists of the transmission of electric energy in interstate commerce is necessary in the public interest, *such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.*" (Emphasis added)

While the MPSC must accept the findings of the FERC with regard to those matters relating to the interstate sale of electricity, this should not affect its duties

to set retail rates. It is these rates which the ratepayers must confront monthly and in ever-increasing amounts. And it is these ratepayers which the legislature sought to protect when it entrusted the MPSC with the responsibility to just and reasonable rates.

A determination of the prudency of expenses recoverable by the utility from its customers through rates is an essential element in rate making. The statute provides that "[T]he Commission shall determine the just and reasonable rates which will yield a fair rate of return . . . ." § 77-3-41, *Miss. Code Ann.* (1972 and 1986 Supp.).

> "A fair return is one which under prudent and economical management *is just and reasonable to both the public and the utility.*"

State Ex. Rel. Allain v. MPSC, 435 So.2d 613 (Miss. 1983).

Appellants have characterized the Mississippi Supreme Court's decision as an attempt to make an independent review of the reasonableness of FERC's allocated cost. However, the Mississippi Supreme Court made it clear that it did not review the reasonableness of the FERC allocation nor look behind the rates established by them. The Federal Power Act does not occupy the entire field of electric regulation and expressly states that Federal Regulation extends only to those matters which are not subject to regulation by the States, 16 U.S.C. § 824(a).

The lesson from *Narragansett* is that the division of regulatory responsibilities between the federal and state governments is neither obscure nor ambiguous. The states

cannot establish rates for utilities' interstate sales nor can the federal government make rates for the retail customer. What MP&L has sought, and the MPSC has ordered, are rates made for the Mississippi retail customer by the Federal Energy Regulatory Commission.

The prudence, or managerial wisdom, of MP&L's undertakings in connection with Grand Gulf is properly within the jurisdiction of the MPSC as it relates to a proposed retail rate increase. The investigation cannot legally conflict with the determination of the FERC of MP&L's allocation of Grand Gulf capacity nor with the wholesale rates to be charged to MP&L by Middle South Energy, Inc., for that power. The investigation by MPSC, however, can and must lawfully be directed at the prudence of MP&L's undertakings with respect to Grand Gulf and the manner and extent to which Grand Gulf expenses are to be recovered from MP&L's customers.

II. STATE REGULATORY ORDER REQUIRING A PRUDENCY HEARING TO DETERMINE WHETHER RETAIL RATES ARE JUST AND REASONABLE, WHERE THE FERC HAS DECIDED WHOLESALE RATES IS NOT PROHIBITED BY THE COMMERCE CLAUSE.

In this case, the Court is asked to decide whether the Commerce Clause of the United States Constitution prohibits a state from conducting a prudency hearing to determine whether retail rates are just and reasonable, where the FERC has decided wholesale rates.

MP&L argues that the effect of the Mississippi Supreme Court Order, mandating that the Mississippi PSC conduct a prudency hearing, is an impermissible burden on interstate commerce. We disagree with their assertion.

The Mississippi PSC is authorized by Mississippi law (*Miss. Code Ann.* § 77-3-39 (1986 Supp.))[1] to establish just and reasonable rates which leads to a fair rate of return for the utility. Pursuant to its statutory authority, a hearing is authorized to determine the reasonableness and lawfulness of such rate changes. Determining whether retail rates to be charged to Mississippi customers are economical and an efficient mix of energy does not constitute a burden on interstate commerce.

The Court has used a two-tiered approach in analyzing whether a state or local regulation violates the Com-

---

[1] *Miss. Code Ann.*, § 77-3-39 (1986 Supp.), §§ (1) & (5):

"(1) Whenever there is filed with the commission by any public utility any notice of intent to change rates pursuant to the provisions of § 77-3-37, the commission, if it so orders within the thirty (30) days after the date such notice of intent is filed, shall hold a hearing to determine the reasonableness and lawfulness of such rate change. The commission shall hold such hearing in every case in which the change in rates constitutes a major change in rates, as defined in § 77-3-37. Provided, however, an abbreviated proceeding may satisfy this requirement if the commission's order is supported by the data, documentation and exhibits on file in the proceeding."

"(5) If, after such hearing, the commission shall find any such rate or rates to be unjust, unreasonable, or unreasonably discriminatory, or in anywise in violation of the law, the same shall be set aside, and the commission shall determine and fix by order such rate or rates as will yield a fair rate of return to the public utility for furnishing service to the public and shall make and file its conclusions and findings of facts supporting such order. A copy of such order shall be served upon the utility in the manner provided in this chapter, and the rates fixed by the commision shall be legal rates until changed as prescribed by this chapter."

merce Clause of the United States Constitution. The general rule is articulated in *Pike v. Bruce Church*, 397 U.S. 137, 25 L.Ed. 2d 174, 90 S.Ct. 844 (1970):

> ". . . Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. *Huran Cement Co. v. Detroit*, 362 U.S. 440, 443, 4 L.Ed.2d 852, 856, 80 S.Ct. 813, 78 ALR 1294. If a legitimate local purpose is found then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities. Occasionally the Court has candidly undertaken a balancing approach in resolving these issues, *Southern Pacific Co. v. Arizona*, 325 U.S. 761, 89 L.Ed. 1915, 65 S.Ct. 1515, but more frequently it has spoken in terms of "direct" and "indirect" effects and burdens. . . ."

MP&L argues that Mississippi's conduct is indistinguishable from what New Hampshire attempted to do in *New England Power Co. v. New Hampshire, supra.* We disagree, in *New England Power, supra,* a New Hampshire statute restricted the export of hydroelectric energy produced within the state, if the Commission determined that the energy was required for use within the state. The Court found that the state imposed burden was prohibited by the Commerce Clause as economic protectionism. In this case, there is no statute which prohibits the exportation of energy out of the state nor is Mississippi PSC attempting to restrict the sale of energy outside the state. By conducting a prudency hearing, Mississippi is attempting to perform its local regulatory function of determining whether intrastate retail rates are just and reasonable. As to those matters not resolved by the FERC, State regulation is not preempted provided that State regulation would not contradict or undermine FERC determinations and federal interests, or impose inconsistent obligations on the utility companies involved. *Appeal of Sinclair Mach. Products, Inc.*, 498 A.2d 696 (N.H. 1985).

The Court in *Arkansas Electric Cooperative v. Arkansas Public Service*, 461 U.S. 375 (1983) in applying the *Bruce Church* test, found that Arkansas PSC regulation of cooperative wholesale rates was permissive and not prohibited by the Commerce Clause. The Court in finding no economic protectionism concluded,

> ". . . state regulation of the wholesale rates charged by AECC to its members is well within the scope of 'legitimate local public interest,' particularly considering that although AECC is tied into an interstate grid, its basic operation consists of supplying power from generating facilities located within the State to member cooperatives, all of which are located within the State. *Cf., Id.*, at 473, n. 17, 66 L.Ed 2d 659, 101 S.Ct. 715. . . ."

Using the analysis of *Arkansas, supra*, determining if local retail rates are reasonable and just has no effect on interstate commerce.

In applying the *Bruce Church* test to the case at bar, the first criteria, the existence of a legitimate local interest, is met. Mississippi has an interest in providing reasonable retail rates to the consumers. The State also has an interest in preventing utility rates from oppressing its citizens, while insuring rates are sufficient to main-

tain reliable service and affording the utility a fair rate of return.

Secondly, one must inquire whether the State regulation at issue, falls more heavily on out-of-state concerns than it does on local business and if it impedes the natural laws of supply and demand. The purpose of the Mississippi Supreme Court in remanding this case to the Mississippi PSC, was to determine whether MP&L is conducting its operation in a prudent manner. When a state statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state interest over out-of-state concerns the court has generally struck down the statute without further inquiry. *Brown-Forman Distillers v. New York State Liquor Authority*, 476 U.S. —, 90 L.Ed.2d 552, 106 S.Ct. —. Clearly, on the face of the Mississippi Statute, the conducting of a prudency hearing has no effect on interstate commerce, inasmuch as the question of intrastate operations is at issue. The prudency hearing, if conducted by the Mississippi PSC, will not interfere with the wholesale rates ordered by the FERC.

CONCLUSION

The decision of the Mississippi Supreme Court should be affirmed. The State's authority to conduct a prudency review to determine just and reasonable retail rates is not precluded by the Federal Power Act.

Respectfully submitted,

JESSE C. PENNINGTON*
Mississippi Legal Services Coalition
Post Office Box 22887
Jackson, Mississippi 39205
(601) 944-0765

LEWIS BURKE
Central Mississippi Legal Services
Post Office Box 52
Vicksburg, Mississippi 39180
(601) 636-8322

Attorneys for Appellees

*Counsel of Record

APPELLEE'S

BRIEF

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

CASES:

TABLE OF AUTHORITIES—Continued

Page

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

STATEMENT OF THE CASE

INTRODUCTION

Appellant, Mississippi Power & Light Company (MP&L or Company) asks this Court to hold that the decision of the Federal Energy Regulatory Commission (FERC) to apportion total Middle South Utility (MSU) system nuclear investment costs to its MSU subsidiary operating companies as wholesale shares of a single system generating plant preempted the jurisdiction of the State of Mississippi to set retail electricity rates. The effect of such a holding would be to create a regulatory gap not contemplated by the Constitution, Congress in adoption of the Federal Power Act, or the authorities of this Court. The regulatory responsibility for the setting of retail electricity rates has been and continues to remain with the states. MP&L has presented no legal arguments or policy reasons to support the substantial departure which it proposes. To the contrary, the very same reasons supporting the line drawn between the regulation of interstate, wholesale sales of electric power and the intrastate, retail sales remain unchanged.

MP&L AND GRAND GULF: STATE ADMINISTRATIVE AND COURT PROCEEDINGS

MP&L is a wholly owned subsidiary of Middle South Utilities, Inc. MSU owns all of the common stock of MP&L (and its sister subsidiary operating and generating companies) and the chief executive officer of MSU controls the voting of all of that stock. MP&L operates in a jurisdiction composed of 45 counties in western Mississippi. Among its 333,000 customers, MP&L provides retail electric service to areas containing some of the poorest people in the United States.

Two counties in the MP&L service area were among the ten poorest in the nation. Of the service area outside

of Hinds County, [illegible] below the pov-erty level in 1979 as compared to 11% throughout the United States. Twenty-eight of the 45 counties receive an 18 to 1 ratio of transfer payments from government sources.[1] The per capital income in 1983 in the service area was $8,210.00, compared to the national figures showing a per capita income of $11,000.00.[2]

Until this rate case, MP&L had constructed and owned the capacity to meet the demand placed upon it by its customers. This was accomplished by the location and construction of oil or gas generated plants throughout the MP&L service area.[3] All of these plants were acquired pursuant to authority granted by the Mississippi Public Service Commission (MPSC). Additionally, the MPSC authorized MP&L to acquire a 25% ownership in the Independence Steam Electric Station (ISES) Units 1 and 2, coal fueled generating facilities located in Arkansas. The total MP&L capacity of 3145 megawatts[4] exceeded its 1985 capacity needs of 1788 megawatts (R. Ex. 2, FFG-4) by 76%.

---

[1]Testimony of Edward L. Ranck, Mississippi State Economist and Assistant Director of Mississippi Research and Development Center. R.3192-5. Citations in the Brief are referenced as follows: "J.S. App." refers to the Appendix to the Jurisdictional Statement; "Supp. App." refers to the Appendix to the Motion to Dismiss; "J.A." refers to the Joint Appendix of the Parties; and "R." refers to the original record which has been lodged with the Clerk of the Court.

[2]The per capita income figures have more dramatic impact when the relatively affluent Jackson Metropolitan Statistical Area including Hinds, Madison and Rankin Counties are removed. When that is done, the census figures reflect 24.1% of the families in the service area below the poverty level with a per capita income of $7,296.00. *Id.* at 3194.

[3]In 1985 MP&L had in operation five oil and gas fired generating facilities located within its territorial jurisdiction. MP&L FERC Form 1, pp. 402-3, year ending December 31, 1985.

[4]*Id.*

In addition to that, MP&L purchased from non-associated utilities during 1985 1,162,872 megawatt hours of energy from non-associated utilities.[5] Not only had MP&L achieved diversity in its mix of sources of power, it had gained access to capacity and energy far in excess of the demand for electricity by its customers.[6]

Grand Gulf was certificated by the MPSC in 1974 as the world's largest nuclear plant of its type. The projected completion dates for the construction of the plant were 1979 for Unit 1 and 1981 for Unit 2. The total costs in 1974 were projected to be about $1.2 Billion for completion of both units of the generating station; however, when Unit 1 went commercial on July 1, 1985, the costs of Grand Gulf Unit 1 alone had exploded to over $3.5 Billion.

From the outset, Grand Gulf was a Middle South system plant. MP&L alone could not finance the construction of the plant. A sister subsidiary, Middle South Energy, (MSE) Inc., now Systems Energy Resources, Inc. (SERI), was created by MSU to finance, own and operate Grand Gulf. The plant was constructed to meet the needs of the entire MSU system and not just the MP&L service area.

The MPSC was concerned about the obligations it was creating for the ratepayers of Mississippi in issuing a Certificate of Necessity and Convenience for a generating plant for which its ratepayers then had no need. In the MP&L and MSE joint petition filed with the MPSC to seek authority to build the plant, the companies acknowledged that the proposed construction, ownership and operation of the Grand Gulf project fell under the purview

---

[5]*Id.* at p. 326A.

[6]MP&L's Assistant Vice President admitted in testimony before the MPSC that with Grand Gulf, the company would have over 100% capacity above demand. R.196.

of Mississippi law, specifically, § 77-3-1, *et seq., Mississippi Code of 1972.* (Supp. App. 1-20) The joint petition also set forth the manner in which the MSU system proposed to construct, operate and allocate the energy and capacity of Grand Gulf to the MSU system operating companies. (Supp. App. 25-39)

The MPSC issued its order on May 29, 1974, granting the MSE and MP&L authority to construct the plant. The order recited the representations of MP&L and MSE that at the appropriate time the MSU System Agreement on file with the FERC would be amended to make MSE a party (Supp. App. at 33) and that the capacity and energy from the plant would be divided among the operating companies pursuant to the MSU System Agreement. That Agreement provided, among other matters, for this methodology for the equalization of the capacity costs in excess of a company's proportionate share among the MSU operating companies.

Completion of the first unit of Grand Gulf was delayed for a variety of reasons and in 1981, MP&L approached the MPSC for authorization to acquire additional capacity. The Company requested acquisition of a 25% ownership interest in the coal-fired ISES plants in Arkansas. Due to heightened public awareness and concern over the escalating costs of the nuclear power plant construction, MP&L was questioned in public hearings regarding the need for such additional capacity in light of the purported imminent commercial operation of Grand Gulf. MP&L was further questioned about a previously undisclosed agreement between the operating companies entitled "Memo of Understanding" dated July 10, 1980, which allocated a fixed 31.63% of Grand Gulf Unit 1 and 43.97% of Unit 2 to MP&L.[7] That allocation methodology was totally at odds with the system methodology originally represented to the MPSC;[8] however, the MP&L president reassured the MPSC as to the extent of its jurisdiction over Grand Gulf and its ability to control costs of electricity to its ratepayers. MP&L President Donald Lutken testified as follows:

> Q. Is this [the] latest memo of understanding regarding the allocation of capability down at Grand Gulf . . .?
>
> A. Mr. Lutken: Yes, sir.
>
> Q. Will the purchases of energy from Grand Gulf require the approval of the Mississippi Public Service Commission?
>
> A. Yes, sir.

(Supp. App. 48)

Mr. Lutken further testified: ". . . [W]e can make these decisions but what I think we are trying to say is this Commission has the final say-so as to what goes into MP&L's rate base, whether it be 19% of Grand Gulf or 33% of it." (Supp. App. 50)

Based on MP&L's assurances, the MPSC granted the certificate for the purchase of an additional 370 megawatts of capacity from the ISES plants on June 19, 1981.

By Mississippi law and application, the MPSC is charged with setting retail rates. A determination of the prudence of expenses recoverable by the utility from its customers through rates is an essential element. The

---

[7] These percentages represented MP&L's proposed ownership of MSE's 90% share of the Grand Gulf plants.

[8] This is graphically documented by the testimony of MP&L officials who projected in 1974 that MP&L would need no more than 19% of Grand Gulf power under the methodology to be used when it went on line. As it turned out, MP&L had no need for any of Grand Gulf when it became operational. (Supp. App. 49-51 and App. 15a.)

statute provides that: "[T]he Commission shall determine the just and reasonable rates which will yield a fair rate of return. . . ." § 77-3-41, *Mississippi Code of 1972.* The Mississippi Supreme Court has defined fair return in *State ex rel. Attorney General v. MPSC*, 435 So.2d 608, 613 (Miss. 1983): "The fair return is one which under prudent and economical management is just and reasonable to both the public and the utility."

In *Mississippi Public Service Commission v. Mississippi Power Company*, 429 So.2d 883, 887 (Miss. 1983), the Mississippi court stated the importance of prudent and economical management as a determinate in specifying a fair rate of return. The end result of this analysis is rates which are just and reasonable to both the public and the utility. Those rates could be "predicated only upon such operating expenses supported by substantial evidence as are actual and necessary." *State ex rel. Attorney General, supra*, at p. 624.

To pay for its anticipated share of Grand Gulf, MP&L filed a rate increase request with the MPSC on November 16, 1984. Its proposed rates included a flexible rider which would reimburse MP&L for either a 19% allocation of Grand Gulf or a 33% allocation depending on the final decision of the MPSC. The 19% allocation was derived from the original understanding between the Company and the MPSC in 1974 and the 33% allocation was derived from the initial decision of the FERC Administrative Law Judge in *Middle South Energy, Inc.*, 26 FERC ¶63,044.

In March, 1985, the MPSC without noti e to the various parties severed the acknowledged issues of prudency and rate design from the rate case. The MPSC took this action in spite of the fact that the prudence of MP&L's capacity was acknowledged to be an issue in the case. The MPSC staff even specified that it was a crucial issue.

(R.47). Subsequently in May of 1985, the parties to the rate request pending before the MPSC stipulated to the methodology for the establishment of rates which would meet the company's revenue requirement without any consideration of the Grand Gulf issues. The issues reserved were prudence, excess capacity resulting from the ISES plants and Grand Gulf, and various issues pertaining to the 1974 certification proceeding before the MPSC for construction of Grand Gulf.

Notwithstanding its failure to address these excluded issues, and in particular the prudence of the expenses associated with Grand Gulf, the MPSC issued a decision in September of 1985, which would ultimately pass through to the retail ratepayers the entire costs and expenses associated with 33% of Grand Gulf Unit 1.

The rate increase for the first year would have totaled approximately $327 Million (a 65% increase over the level of rates approved by the MPSC on June 14, 1985, J.S. App. 41a, 42a) however the MPSC acted to ameliorate the massive rate increase by adopting a two-phase rate moderation plan. Under the plan, the impact on ratepayers amounting to a cumulative increase of 50%, was to be introduced over a five year period. The order provided for the following increases:

Year	Annual Increase Ordered	Cumulative Increase Over 1984 Rates
1985-86	14.07%	14.07%
1986-87	8-10%	22-24%
1987-88	8-10%	30-34%
1988-89	7- 8%	37-42%
1989-90	7- 8%	44-50%

Even with the rate moderation plan these rates for MP&L customers for the winter months of 1986 and 1987 ranked as the 50th highest costs when compared with 191

service territories of the major regulated electric utilities in 49 states and the District of Columbia.[9]

The decision of the MPSC was appealed to the Mississippi Supreme Court. That court reversed the decision of the MPSC and remanded it to the MPSC:

> In remanding this case to the MPSC for a review of the prudency of the Grand Gulf investment, we rely on the expertise of this agency in making a determination of whether MSU and its subsidiaries made reasonable decisions in light of local conditions. *We believe that this is a matter best left to the state agency to resolve and that this issue has not been preempted by federal jurisdiction over interstate wholesale ratemaking.* (Emphasis Supplied)

(J.S. App. at 18a, 19a) The Mississippi court decided that the issue reserved by this Court in the *Nantahala Power & Light Co. v. Thornburg*, No. 85-568, 106 S.Ct. 2349 (June 17, 1986) decision with regard to the availability of power at a lower cost than that which is FERC-approved was applicable to this case where there appeared in the record evidence of such sources. (J.S. App. 15a) The decision of the Mississippi Supreme Court

[9]Rodgers, Foley and Lehman, "Residential Electric Bills, Winter 1986-87", National Association of Regulatory Utility Commissioners, pp. 199-201 (Dec. 31, 1987). The nationwide rankings were based upon 500 kwh consumption per month. Within the context of the ranking of rates, MP&L would not be the "best friend" that MP&L ratepayers ever had. When counsel in the *Nantahala* presented oral argument to this Court on April 21, 1986, he characterized Alcoa as the best friend that North Carolina ever had because it provided the lowest rates in North Carolina. The MP&L rates are substantially higher than those paid by Mississippi customers of the other major investor owned utility in the state. Furthermore, it must be remembered that during this period only 14.5% of the actual costs of Grand Gulf were reflected in these rates. The remaining 85.5% had been deferred for future recovery and were accumulating an additional interest to be paid by MP&L customers. (J.S. App. at 46a)

did not foreclose the MPSC from making any decision nor did it foreordain any decision in its reversal. In its remand, the court specifically held that "... this is a matter best left to this state agency to resolve." (J.S. App. 19a)

MP&L AND THE MIDDLE SOUTH SYSTEM: THE FERC PROCEEDINGS

In 1982, the MSU system filed two intra system contracts with the FERC for approval. The first was styled the Unit Power Sales Agreement (UPSA). It was filed by MSE and contained an allocation of Grand Gulf based on the earlier "Memo of Understanding" executed by the MSU operating companies. A second case was filed by the service company subsidiary for the MSU system, Middle South Services, Inc. (MSS), which involved several changes to the 1973 System Agreement. The most significant change was to alter the method of equalizing the costs of excess capacity on the MSU system. The method of allocation of Grand Gulf to the various jurisdictions became the central issue in both cases.

The administrative law judge assigned to the case involving the UPSA[10] found that it perpetuated discrimination which would result in serious detriment to the ratepayers of Mississippi who would pay about four times more for nuclear capacity than Arkansas ratepayers. (26 FERC ¶63,044 at p. 65,107.) The remedy decided by the administrative law judge was to equalize all nuclear generating capacity investment costs among the MSU operating companies. Illogically, the decision resulted in an increase in MP&L's allocation of Grand Gulf Unit 1 from 31.63% as set out in the Memo of Understanding to 33%.

[10]*Middle South Energy Inc.*, 26 FERC ¶ 63,044.

Parallel to the hearings and decision on the UPSA were hearings conducted on the proposed amendments to the System Agreement.[11] A different administrative law judge heard that matter and held that the method of creation and the proposed operation of Grand Gulf was an anomoly among the generating plants on the MSU system. He decided the remedy to be that the Grand Gulf plant should be divided among the MSU operating companies based upon the average annual energy demand or total energy usage on the MSU system. The effect of that decision would have been for MP&L to receive an allocation of approximately 15% of the capacity and energy of Grand Gulf.

After receiving these two administrative law decisions based on exceptions filed by the various parties, the FERC issued a consolidated order on January 13, 1985, in which it attempted to resolve the issues in both cases. *Middle South Energy, Inc.*, 31 FERC ¶ 61,305. The FERC adopted the decision of the Administrative Law Judge deciding the UPSA matter and MP&L thus ended up with 33% of Grand Gulf. After granting rehearing, the FERC clarified its initial order by opinion and order issued on September 26, 1985. *Middle South Energy, Inc.*, on rehearing, 32 FERC ¶ 61,425. The FERC made no substantial changes in its earlier decision.[12]

---

[11] *Middle South Services, Inc.*, 30 FERC ¶ 63,030.

[12] Sixteen of the parties before the FERC in these proceedings noticed and prosecuted appeals to the Circuit Court of Appeals for the District of Columbia *sub nom, Mississippi Industries, et al. v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987). The panel decision affirmed the FERC opinion and a dissenting opinion by Judge Bork was filed. After the court *en banc* granted rehearing, the original panel *sua sponte* reversed itself and returned the case to the FERC. 822 F.2d 1104 (D.C. Cir. 1987). On November 30, 1987, the FERC issued its decision in which

(Continued on following page)

A considerable amount of proof at the FERC hearings related to the question of the degree of integration of the MSU system. The underpinning of the FERC decisions to impose on the operating companies a share of the costs Grand Gulf (and other nuclear generating plants) was that the MSU system was sufficiently integrated to justify a systemwide division. While the FERC did find that the MSU system was integrated and in a power pooling arrangement, it did not find it to be a single, monolithic entity. The Opinion on Rehearing, 234A, held the following:

> Both AI and the cities of Benton et al., question whether the Commission intends the term "single system" to mean "a group of utilities that have submerged their separate identities, and the interests of their native-load ratepayers into a common, homogeneous physical and economic unit that is indistinguishable from a single utility."
>
> We think it obvious from Opinion No. 234 that the Commission did not intend a meaning such as that quoted above. The opinion does not describe the MSU system as a "monolithic" entity nor does it ignore certain autonomous aspects of the individual operating companies. (Footnotes omitted)

(32 FERC ¶ 61,425 at p. 61,952; J.S. App. 173a). The opinion further stated:

> In reaching the above conclusion, the opinion repeatedly recognizes that the individual operating companies are intimately involved in the planning stages of new generation units on the System. It further recognizes that the Operating Committee (which is composed of representatives of the individual operating companies) makes major System decisions in the form of recommendations to the chief executive offi-

---

(Continued from previous page)

it reaffirmed the Grand Gulf I cost allocation of its decisions in FERC Opinions 234 and 234-A. Petitions for rehearing are pending at this time.

> cers who, in turn, vote on the recommendations, and that the individual companies make the final specific decisions necessary to carry out the overall system plan. [Noting for example, specific timing and location of new generation].

(32 FERC ¶ 61,425 at p. 61,953; J.S. App. 174a)

The FERC was very specific about what its opinion did not decide regarding the autonomy of the individual operating companies.

> The Arkansas parties are incorrect that our decision was made without regard to ownership and financing of generating units. The opinion explicitly recognized, 31 FERC at pp. 61,649 and 650 that each operating company is required by the System Agreement to own or purchase capacity to meet native load. *We also recognize, although it was not emphasized in the opinion, that pool members have first call on the power and energy produced by units which they now own.* All of these factors were important considerations in our decision not to adopt full production cost equalization, and, to the greatest extent possible, to allow the individual companies to retain the benefits of units which they have been responsible for constructing. (Emphasis added)

(32 FERC ¶61,425 at p. 61,955; J.S. App. 176a, 177a)

MP&L'S EXCESS CAPACITY AND THE ABSENCE OF A PRUDENCY REVIEW

The record before the Mississippi Supreme Court reflected that with the purchase of power from the coal generated ISES units in Arkansas, MP&L had 85% over its peak demand in Mississippi in August of 1985. With 33% of Grand Gulf, MP&L had over 100% of its peak demand for its energy. (J.S. App. 9a) Likewise, the record indicated that MP&L had no plans to either retire any of its base load capacity, or reduce its maintenance and operation cost on those units. (R.1230)

MP&L had the highest excess capacity of any of Middle South Utilities' affiliates and as much as 1108 megawatts were being sold off each month to the other MSU companies. This excess energy was being sold, however, not at the cost of production, but at the price of the older oil and gas capacity costs. (J.S. App. 15a)

MP&L responded to challenges about its available capacity by stating that the large capacity reserve was designed to meet the systemwide demand, as well as to provide for diversity in the baseload capacity, which was, in its opinion, a more reliable long-range base. The Mississippi Supreme Court concluded that the legal responsibility for determining the long range needs for Mississippi ratepayers as well as what just and reasonable retail rates they should pay, remained with the MPSC. *Accord, Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Commission*, 461 U.S. 190 (1983).

The prudence of MP&L's decision to enter into the agreements resulting in a 33% ownership of the Grand Gulf plant has never been determined. It is undisputed that no prudency review was conducted by the MPSC.[13] The FERC likewise has made no determination of the prudency of MP&L's excess capacity. The FERC administrative law judge in the UPSA case specifically excluded consideration of prudency at the retail level.

> PRESIDING JUDGE: I don't think I or the Commission will ever do that, in other words, make a finding saying "Here are our determinations about prudency and they govern retail rates and everything else.

(FERC, Docket No. ER-616-000, Supp. App. 63) *See, also*, statements of Administrative Law Judge Liebman to the same effect at Supp. App. pp. 59,60,61,63,66.

---

[13]This was stated to the Mississippi Supreme Court by the MPSC in oral argument.

The FERC in its opinion on rehearing expressed its intention not to interfere with the traditional roles of the states in setting retail rates. "What our decision attempts to do is amend the filed agreements to achieve a non-discriminatory sharing of excess capacity cost imbalance on the integrated system, consistent with the goal of the System Agreement and to do so with as little intrusion on the states as possible." (32 FERC ¶ 61,425 at p. 61,952)

The chairman of the FERC in testimony before Congress responded to a question whether the FERC considered the prudence of the purchaser of power as being within the scope of the issues it considered in reviewing rates. The Commission chairman stated, "Our interpretation of the law has been that the proper forum for reviewing the purchaser utility's prudence in entering into the purchase is properly lodged in the State forum."[14]

Nearly a year later, the FERC Acting Chairman Anthony Sousa, responded to questions posed by the chairman of a congressional committee. He was asked,

> Please describe the Commission's efforts to determine the prudency of the purchase of power by any of the Mississippi South Utilities affiliated companies from the Grand Gulf Nuclear Power Plant. Please state why Opinions 234 and 234A do not address the prudence of such purchases, including need for power, the impact on the ultimate consumers and available alternatives.

His answer was, "The Commission did not determine the prudence of the purchase of power by the Middle South Utilities from the Grand Gulf Nuclear Generating Station. Opinion Nos. 234 and 234-A."[15]

[14]*Hearings Before the Subcommittee on Energy Conservation and Power of the Committee on Energy and Commerce,* House of Representatives, 99th Cong., Ser. No. 15, 1st Sess., 542 (1985) (Statement of Raymond J. O'Connor, Chairman, Federal Energy Regulatory Commission).

After the FERC allocation was ordered on June 13, 1985 in Opinion 234, all of the operating companies requested retail rate increases to reflect their shares of Grand Gulf. As a result of these retail rate proceedings, MP&L is the only retail jurisdiction that has not absorbed some of its portion of Grand Gulf's construction and operating costs.[16] As part of the resolution of the rate increase sought by LP&L for its nuclear generating plant, Waterford 3, and for its 14% share of Grand Gulf, LP&L agreed to permanently retain 18% of its share of Grand Gulf 1. In addition, the LPSC has conducted prudency investigations into LP&L's Grand Gulf involvement.[17]

Likewise, New Orleans Public Service, Inc., (NOPSI) entered into an agreement with the City Council of New Orleans in which it agreed to permanently absorb $51.2 Million in Grand Gulf costs, and acknowledged that the Council could proceed with a prudency inquiry into the recovery of Grand Gulf costs.[18]

Arkansas Power & Light entered into an agreement whereby it would permanently retain a portion of its 36%

[15]Letter from Anthony G. Sousa, Acting Chairman FERC to Edward J. Markey, Chairman, Subcommittee on Energy and Power, Committee on Energy and Commerce, U. S. House of Representatives, March 14, 1986, Question No. 11 and answer. This statement stands in stark contrast to the assertions of MP&L (Appellant's Brief pp. 13-14) and Amici Solicitor General and FERC (Brief, p. 19) that FERC has in some manner, ruled on the prudency issue.

[16]Form 10-K, Securities and Exchange Commission, Annual Report of Middle South Utilities, Inc., operating companies, December 31, 1986, p. 36.

[17]*Id.* at 32.

[18]*Id.* at 40.

allocated share of Grand Gulf 1 which is its "retained share." This share ranges from 4.32% in year one to 7.92% in year nine and all subsequent years.[19]

These two prudence investigations and retentions of at least some of the other operating companies' expenses for Grand Gulf related cost are precisely what MP&L, their sister subsidiary, claims the MPSC should be preempted from performing in the instant cause.[20]

SUMMARY OF ARGUMENT

The Appellant Has Presented No Question for Review Which Satisfies the Finality Requirement of 28 U.S.C. § 1257.

The Mississippi Court heard the appeal from an order of the MPSC which had failed to comply with the requirements of state law when it failed to determine the prudency of the expenses being passed on as rates to the retail consumers. The Mississippi court returned the case to the MPSC so that the state agency could determine the prudency and reasonableness of expenses for which MP&L requested reimbursement by retail rates in the light of the availability of other lower cost sources of power and excess capacity, among other issues. Until the MPSC has acted upon the remanded case, this Court is not presented questions which have been finally resolved. *North Dakota Pharmacy Board v. Snyder's Stores*, 414 U.S. 156 (1973).

Nor has MP&L presented any exceptional circumstances which justify this Court's departure from its finality requirement. *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975). Despite the claims of MP&L, the order

[19]*Id.* at 26.

[20]NOPSI has reserved its rights to raise jurisdictional issues. Form 10-K Securities and Exchange Commission 1986, pp. 41-2.

of remand by the Mississippi court to the MPSC does not foreclose it from collecting Grand Gulf expenses as retail rates. Mississippi law specifically provides for the recovery of any expenses which can be justified as an emergency. § 77-3-41, *Mississippi Code of 1972*. The MPSC is in the best position to determine the validity of the claims of MP&L that without the collection of these rates, it will suffer irreparable harm. It is in that forum that the financial and legal interests of the company and the public can best be balanced.

The claims of MP&L that the MPSC is preempted from considering the issues of prudency under the Federal Power Act do not satisfy a second exception to the finality requirement of 28 U.S.C. § 1257. To succeed, MP&L would have to demonstrate that the preemption issue could be separated from the merits of the Mississippi court's state law considerations. *Construction Laborers v. Curry*, 371 U.S. 452 (1963). In its remand to the MPSC, the Mississippi court adhered to well-settled principles of state and federal law. No legitimate federal policy is eroded by the Mississippi decision.

Federal Power Act Preemption & Public Policy Consideration

MP&L contends that the MPSC is preempted from conducting an inquiry of the reasonableness and prudency of the Grand Gulf expense which MP&L wants to collect as retail rates. While it is clear that the MPSC cannot substitute its judgment for that properly exercised by the FERC, nor can it set wholesale rates, it is equally clear that the state agency must consider the reasonableness of the costs incurred by MP&L which it desires to pass on as retail rates. It may determine whether MP&L has acquired excess capacity which would unreasonably burden the retail ratepayers and whether or not there are sources

of lower cost power available to MP&L which would reduce the burden of the retail ratepayers. It can also determine if other savings exist that could offset the impact of Grand Gulf on MP&L's revenue requirement. This does not defeat the jurisdiction of the FERC but, to the contrary, fulfills the authority of the states expressly reserved by the Federal Power Act.

It is certain that the FERC has no authority over generation facilities which are certificated by the states. There is a substantial question that the FERC was within its jurisdiction to allocate Grand Gulf 1 which had been certificated by Mississippi. While that question is not presented here for review, the preemption argument advanced by MP&L rests exclusively on the legality of that FERC decision. That question should be resolved before the MPSC is barred from carrying out its duties under state law.

Acceptance of the argument that the MPSC cannot investigate the prudency of the Grand Gulf expense will create a regulatory gap not contemplated by the FPA. The FERC did not investigate the prudency of Grand Gulf expenses for retail ratemaking purposes. Moreover, the FERC is not charged with nor prepared to carry out the duty to determine the circumstances of local conditions properly considered in the retail ratemaking process.

The *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 106 S.Ct. 3268, 90 L.Ed.2d 943 (1986) decision, consistent with the Court's earlier decisions and the decisions of state courts, recognizes the dual regulatory system and the duty of the states to set retail rates. The *Nantahala* opinion considered the rights of the states to make selections from various sources of power which might be available to them to achieve economies for the retail ratemakers.

Commerce Clause

The MPSC has made no decision after the Mississippi Court remand to take all or none of the allocation of Grand Gulf. MP&L claims that if the MPSC decided to order as retail rates less than the entire allocation of MP&L of Grand Gulf, it would be a *per se* violation of the Commerce Clause. In making a decision, the MPSC is not directed by Mississippi statute nor the remand order of the Mississippi court to embargo lower costs energy to its Mississippi ratepayers at the expense of those from other states.

Applying the balancing test in *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970) for Commerce Clause violation analysis, MP&L claims that Mississippi's legitimate interests are being fully protected by the FERC. There is no evid[illegible] that the FERC gave any consideration to the impact of these rates on Mississippi's ratepayers. The FERC has not considered the economical mix of high and low cost electric power available to the Mississippi retail customers; nor has it considered the local conditions of the Mississippi retail ratepayer with respect to the economic conditions familiar to the MPSC.

Equitable Estoppel

Because of prior representations made to the State of Mississippi, the Court should apply the historic doctrine of equitable estoppel to prohibit MP&L from now claiming federal preemption of further state actions by Mississippi and, specifically, the state prudency review mandated by the Mississippi Supreme Court.

MP&L and its sister subsidiary MSE, in order to receive the necessary license to construct the Grand Gulf Plant in 1974, represented to the state's utility regulatory agency, the MPSC, that the construction and operation of the plant came within the purview of Mississippi's Public

Utility Act of 1956 codified as §§ 77-3-1, *et seq.*, *Mississippi Code of 1972*. Additionally, the companies represented a specific allocation methodology that the MSU system would seek to have incorporated in the MSU System Agreement on file with the Federal Power Commission.

The MSU operating companies subsequently entered into secret deliberations as to a different allocation methodology for the Grand Gulf Plant in 1977. The state was never informed that different allocation methods for the plant were being discussed within the MSU System. In 1981, in MPSC hearings regarding MP&L's request to purchase additional capacity from the coal fired ISES in Arkansas, the MP&L president was confronted with a "Memorandum of Understanding" signed by the presidents of the various MSU operating companies a year earlier which gave MP&L a fixed allocation of 31.63% of Grand Gulf Unit I. That fixed share of Grand Gulf was based on an allocation methodology totally different from that originally represented to the MPSC.

When questioned about the impact of the memorandum, the MP&L president hastened to reassure the state officials that the MPSC still had the ultimate jurisdiction and authority as to the retail rates to result from the Grand Gulf Plant.

There can be no doubt that the prerequisites to the doctrine of equitable estoppel have been satisfied. The state has relied to its detriment on the truth of the various representations made by MP&L and MSE. The state allowed the Grand Gulf construction to proceed and its citizens now face paying for 33% of the plant if MP&L's arguments prevail. Further, the MPSC has allowed MP&L to even purchase additional capacity from the ISES plant in

Arkansas adding to the Company's excessive generating reserve margin.

The representations made by MP&L, and MSE were recited by the Mississippi Supreme Court as an important component of its decision below. Additionally, the same representations were found to warrant the application of the doctrine to MSE by the U. S. District Court for the Southern District of Mississippi when MSE sought to enjoin the MPSC from auditing its records. That court held that MSE was bound by its representations in 1974 that it came under the purview of Mississippi's Public Utility Act of 1956 and required the company to open its financial records to the MPSC for a financial audit.

ARGUMENT

MP&L seeks reversal of a state court which directed its administrative agency to apply legally required standards to set retail rates. Facially, MP&L urges the Court to invade the well-defined jurisdiction of the State of Mississippi; but MP&L contends that because the FERC approved a contract between MP&L and its sister subsidiaries for the allocation of ownership interest of Grand Gulf, the authority of the MPSC to set retail rates has been preempted. This reasoning again ignores the distinction between federal and state jurisdiction over utility ratemaking and the dual regulatory system deeply implanted in our jurisprudence. Adoption as law of the argument advanced by MP&L would reverse settled law, ignore the administrative decisions of the FERC, and create a regulatory gap which would leave the retail ratepayers without a meaningful opportunity to have their local conditions considered in the retail ratemaking process. Such a decision would, in fact, result in the elimina-

tion of the final step of regulation of a monopoly, leaving to the Company's economic conscience to choose between absorbing its risks of managerial imprudence or passing the costs of those risks to its captive customers.

A. The Order Being Reviewed On Appeal Was Not Final Under 28 U.S.C. § 1257 and This Court Has No Jurisdiction At This Time.

This Court's appellate jurisdiction is limited to "[f]inal judgments or decrees rendered by the highest court of the State in which a decision could be had . . ." 28 U.S.C. § 1257(b). As this Court stated in *North Dakota Pharmacy Board v. Snyder's Stores*, 414 U.S. 156 (1973), the finality requirement contained in 28 U.S.C. § 1257 serves several important purposes:

> (1) it avoids piecemeal review by federal courts of state court decisions; (2) it avoids giving advisory opinions in cases where there may be no real "case" or "controversy" in the sense of Art III; (3) it limits federal review of state court determinations of federal constitutional issues to leave at a minimum federal intrusion in state affairs.

Id. at 159.

In several limited instances, this Court has departed from the requirement of strict finality in exercising its appellate review of the decisions of a state high court when further disposition of the action will occur in the lower state courts below. In *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975), this Court cited four categories of cases in which a state court's decision on a federal issue has been treated as final even though further proceedings are anticipated in the lower state's judicial or administrative bodies. The two categories relied on by MP&L are as follows:

> "Cases . . . in which the federal issue, finally decided by the highest court in the state, will survive and require a decision regardless of the outcome of further state court proceedings."

420 U.S. at 480.

> Cases "where the federal issue has been finally decided in the state courts with further proceedings pending in which the party seeking review here might prevail on the merits on non-federal grounds, thus rendering unnecessary review of the federal issue by this Court, and where reversal of the state court on the federal issue would be preclusive of any further litigation on the relevant cause of action rather than merely controlling the nature and character of, or determining the admissibility of evidence in, the state proceedings still to come." In this category this Court has looked to see if an important federal policy would be eroded if the appeal were not immediately entertained.

420 U.S. at 482-83. For the reasons that follow, it is submitted that MP&L has misapprehended these two *Cox* categories and, therefore, the appeal should be dismissed for lack of finality.

Under the second *Cox* category, the state court must have decided the federal issue and at the same time, it must be an issue which will survive and require decision regardless of the outcome of further state court proceedings. 480 U.S. at 479. In announcing this particular exception to finality, this Court in *Cox* relied on two of its previous decisions: *Radio Station WOW, Inc. v. Johnson*, 326 U.S. 120 (1945) and *Brady v. Maryland*, 373 U.S. 83 (1963). Both of these earlier decisions were concerned about irreparable injury occurring to the party seeking review if the appeal had not been granted.

In the case now before the Court, the circumstances presented here remove this case from the second *Cox* exception. Notably, there is a provision in the Mississippi

statutes which allows for emergency rate relief. § 77-3-41, *Mississippi Code of 1972* Accordingly, the "immediate and irreparable consequences" that MP&L contends exist now on account of the Mississippi Supreme Court's decision can be easily addressed and rectified by utilizing the statutory provision for emergency relief and will protect MP&L, assuming it can justify its claims. There is nothing contained in the Mississippi statutes or the state court's decision which would require refund of the rates collected by MP&L.

MP&L alleges in footnote 26 p. 29 of its brief that "the Mississippi Supreme Court repeatedly stated that MP&L does not 'need' any of the Grand Gulf I power and that it is imprudent for MP&L to have 'purchased' such expensive power when MP&L has 'excess capacity' without the Grand Gulf I allocation, and when MP&L's native capacity is cheaper than Grand Gulf I." This characterization of the state court's ruling is simply not so. All that the Mississippi Supreme Court said was that since the ratepayers in Mississippi cannot use 33% of Grand Gulf's power, the 1982 System Agreement providing for the allocation of 33% of its cost would "*seem*" to be imprudent. (Emphasis added) (J.S. App. 16a)

MP&L contends that the stay orders previously entered by this Court "establish that compliance with the Mississippi 'transfer' orders (the roll-back and refund) will irreparably harm MP&L." In this regard, this Court simply required that MP&L post a bond under the conditions previously set by the Mississippi Supreme Court. Accordingly, this Court's entry of stay orders should not serve as any indication that this Court has found a likelihood of irreparable harm falling on MP&L should the instant appeal not be entertained by this Court.

The state court simply returned the case to the MPSC relying on the expertise of that agency to determine, among other things, whether MP&L had demonstrated prudent and economical management in its mix of costs of the energy to be paid for by the retail rate payers, in light of the availability of lower cost energy from alternative sources. (507 So.2d 978, 987; J.S. App. 18a, 19a)

Despite what MP&L and Amici Solicitor General and the FERC try to convey, the state court did not decide the issue of prudency, but held that the MPSC had the authority as well as the obligation to make the decision. On this point, this Court in *Nantahala* and the Mississippi Supreme Court are in agreement. As stated by the Court in *Nantahala:*

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though the higher cost power actually purchased is obtained at a FERC-approved, and, therefore, reasonable *price*. (Emphasis in original).

Nantahala, 90 L.Ed2d at 958.

On remand, the MPSC is required to examine every expense chargeable as rates to the consumer to determine if that expense was incurred as a result of prudent or economical management.[21]

On further proceedings, the MPSC can, upon adequate proof, determine that the purchase of the total costs associated with Grand Gulf are just, reasonable and prudently

[21] As described in his treatise, this determination has become so important in modern ratemaking that operating expenses often will be considered before rate base or rate of return. 1 A.J.G. Priest, *Principles of Public Utility Regulation*, 46 (1969).

incurred and could be charged in retail rates. At the same time, the proof might show and the MPSC could conclude that MP&L had available to it adequate supplies of lower cost electricity and that some amount of the energy from Grand Gulf, less than the total amount owned by MP&L, would be included in the retail rates. Asked differently, was MP&L imprudent in entering into contracts acquiring the excessive amounts of capacity? Similarly, the MPSC may also determine that from the panoply of expenses incurred by MJ&L, there are areas which, when combined with the Grand Gulf costs, result in a reduction of the impact of the higher nuclear costs. *Nantahala, supra*, 90 L.Ed.2d at 955; *Narragansett Electric Company v. Burke*, 119 R.I. 559, 381 A.2d 1358 (1977). Simply put, compliance with Mississippi's utility statutes and the fundamentals of proper rate making on the part of the MPSC would in none of the foregoing alternatives draw into question the cost of energy and capacity for Grand Gulf as set by FERC.

In sum, it is not clear that the federal issue, finally decided by the Mississippi Supreme Court, will survive and require decision regardless of the outcome of the further MPSC proceedings. 420 U.S. at 480. Among the decisions which the MPSC can make in this case and which would be subject to review by the state court, the issue raised by MP&L here will be preserved. See *Radio Station WOW, supra*, 326 U.S. at 127. There is no conceivable way that the MPSC could separate from its considerations the Grand Gulf energy and capacity allocated by the FERC to M&PL, simply because that is the principal reason for the rate increase sought by MP&L. As previously stated, the MPSC could arrive at a disposition of the rate increase request which would "make unnecessary [the] decision on the federal question." *Cox supra*,

420 U.S. at 480. The question raised on appeal, therefore, does not fall within the second category of exceptions to the finality requirement.

The appellant also argues that the fourth *Cox Broadcasting* exception for finality exists. So as to allow the Court to hear the appeal under the fourth *Cox* factor, the major consideration of this Court is whether or not the refusal to immediately review the state court decision "might erode federal policy . . . " 420 U.S. at 483. Citing *Construction Laborers v. Curry*, 371 U.S. 542 (1963), MP&L would have this Court believe that merely because it has alleged that the MPSC is preempted from considering prudence issues under the Federal Power Act, then it is entitled to have its appeal entertained under this fourth *Cox Broadcasting* factor. A closer review of the *Curry* decision, however, indicates that the Court found the preemption issue entirely separable and ripe for review.

Alternatively, the *Curry* court noted that the only defense available to the union was the argument of preemption under the National Labor Relations Act. In the instant case, it simply is not clear whether the preemption issue can be separated from the merits of the Mississippi Court's state law considerations.

Notably, it has long been recognized that in the area of the regulation of electrical power, a dual system exists. Under the Federal Power Act, 16 U.S.C. §§ 824 *et seq.* (1982) the FERC has been given exclusive regulatory power over wholesale rates for electricity transmitted and sold in interstate commerce. At the same time, the states have retained "their traditional responsibility in the field of regulating electrical utilities for determining questions of need, reliability, cost and other related concerns"

"[w]ith the exception of the broad authority of the . . . Federal Energy Regulatory Commission over the need for and pricing of electrical power transmitted in interstate commerce . . ." *Pacific Gas, supra* at 205.

Nowhere in the decision of the Mississippi court is it ordered that MPSC is not to give binding effect to the FERC order allocating Grand Gulf costs. Making these choices from those available clearly is a state regulatory function and in no way interferes with the FERC decision to allocate Grand Gulf costs to the subsidiaries of Middle South Utilities.

Accordingly, *Cox's* fourth categorical exception to finality is not satisfied under one circumstance presented in the instant appeal.

B. The Supremacy Clause Does Not Preclude the Mississippi Public Service Commission From Determining MP&L's Managerial Prudence in Setting Retail Rates.

It cannot be disputed that the prudency issues relating to Grand Gulf were expressly excluded from consideration by the MPSC and the MPSC adopted retail rates regarding Grand Gulf without considering the prudency issues. The MPSC acknowledged to the Mississippi Supreme Court that it had not made any findings with regard to prudency when it set the retail rates now in effect.[22] The Mississippi Supreme Court did not hold or make any findings that the decision of MP&L to enter into

[22]The March 5, 1985 order of the MPSC severing the prudency issue was entered *sua sponte* by the MPSC. A stipulation was then entered to permit the ratemaking process to proceed without incorporating any Grand Gulf issues. At the time of the stipulation, the allocation of Grand Gulf was the subject of two differing FERC administrative law judge decisions, one granting 33% of Grand Gulf to MP&L and the other 14.5%. The stipulation gave MP&L the opportunity to seek rate relief on

(Continued on following page)

the Grand Gulf contract was imprudent, nor did it instruct the MPSC on remand to make any findings of imprudency.

The opinion of the Mississippi court was in response to MP&L's contentions rather than a holding on the issue of prudency itself. The Mississippi court had before it a decision of the MPSC which had failed to exercise its duty, including a determination of prudency. MP&L argued that the MPSC was constitutionally precluded from making an investigation of imprudency. A fair reading of the decision here on appeal plainly supports that conclusion. "We are aware of the effect that wholesale rates have on retail rates and we do not challenge the FERC's jurisdiction over interstate wholesale rates." (J.S. App. 14a-15a) The Mississippi court adopted language from *Appeal of Sinclair Machine Products, Inc.*, 498 A.2d 696 (N.H. 1985) which acknowledged that "state regulation is not preempted provided that state regulation would not contradict or undermine FERC determinations in federal interests . . ." (*Id.* at 704; J.S.App. 17a)

MP&L clings to several observations made by the Mississippi court to bolster its argument that the FERC's jurisdiction was invaded. Brief of Appellant, pp. 19-20. Those statements as used by the appellant are not essential to the decision of the Mississippi court and are hence *obiter dictum*. See, *Railroad Company v. Schutte*, 103 U.S. 118 (1881)[23]

(Continued from previous page)

other grounds, while all parties awaited the decision of the FERC. When it made its final decision on the allocation of Grand Gulf, the MPSC simply disregarded its duty to determine the fundamental elements of retail ratemaking. That, of course, was one of the grounds for reversal by the Mississippi Supreme Court.

[23]Since none of the hearings in this matter proceeded with proof related to the prudency issues, the record before the Mis-

(Continued on following page)

The foundation for MP&L's argument is the decision of the Supreme Court of Rhode Island in *Narragansett Electric Company v. Burke*, 381 A.2d 1358 (R.I. 1977), *cert. den.* 435 U.S. 972 (1978). In addition to analysis of the *Narragansett* decision, it is useful to examine the jurisprudence leading to *Narragansett* and its evolution thereafter.

Prior to federal legislation, the Court applying the Commerce Clause held that the states were not prohibited from regulating the sale of gas to retail consumers, even though the gas had traveled interstate. See *Public Utilities Commission v. Landon*, 249 U.S. 236 (1919); *Pennsylvania Gas Company v. Public Service Commission*, 252 U.S. 23 (1920). In deciding what limitations should be placed on state power, the Court held that a state could not regulate wholesale sales of gas in interstate commerce, but it could regulate sales sold to the retail customer. *Missouri v. Kansas Gas Company*, 265 U.S. 298 (1924). In *Public Utilities Commission v. Attleboro Steam and Electric Company*, 273 U.S. 83 (1927), the Court held that regulation of rates charged to the ultimate consumer was intrastate and subject to state regulation while rates charged to a wholesale purchaser were not subject to state regulation.

(Continued from previous page)

sissippi court was much too incomplete for that court to make any findings on prudency, excess capacity or the other matters reserved by order of the MPSC. The information upon which the court based the observations to which MP&L cites are found in the record but were brought out only tangential to the matter being considered by the MPSC. The prefiled testimony of MP&L contained some of the references since several of the prudency issues were to come up at a later time. During the hearings, some allusions were made to these subjects but usually in other contexts. It is nevertheless understood that the MPSC never relied on these when issuing its final order, nor was there any effort by any party to formally address these issues once the order of severance had been issued.

In 1935, Congress assumed its responsible position in this matter by adopting the Federal Power Act, 16 U.S.C. §§ 824a, *et seq.* The purpose of the legislation was to recognize that since the states had the constitutional power to regulate retail sales, but not wholesale, the latter would be unregulated unless Congress filled the void.[24] Congress adopted the standard stated in the *Attleboro* case which created state regulation of a sale at "local retail rates to ultimate consumers", *Illinois Gas Co. v. Public Serv. Co.*, 314 U.S. 498, 504. A case-by-case analysis was eschewed for the "bright line", more mechanical test. *Federal Power Commission v. Southern Cal. Edison Company*, 376 U.S. 205, 216 (1964).

The Mississippi Supreme Court has a consistent record of deferring to the jurisdiction of federal administrative utility regulatory agencies in recognition of the line between retail and wholesale retail regulation. *United Gas Pipeline v. Willmut Gas and Oil Company*, 97 So.2d 530 (Miss. 1957); *United Gas Corporation v. Mississippi Public Service Commission*, 127 So.2d 404 (Miss. 1961). The latter case served as a principal authority in the *Narragansett* decision.

In the *United Gas Corporation v. Mississippi Public Service Commission* decision, the MPSC attempted to regulate the rates being charged by the wholesaler (pipeliner) to its local subsidiary. The sole source of the gas which was sold in retail to its ultimate customers came from its affiliated pipeline company. When the local company requested approval to charge its customer the rate that it had been charged at wholesale, the MPSC refused. The Mississippi court reversed, holding that the rate

---

[24]See, discussion of congressional intent in *Federal Power Commission v. Southern Cal. Edison Company*, 376 U.S. 205, 213 (1964).

charged by the parent to its subsidiary was within the exclusive jurisdiction of the Federal Power Commission and that the MPSC could not look behind that without offending an area of regulation preempted by the Congress.

The only commodity being sold by the retailer was gas and the only supplier of that gas was the one pipeline. The Mississippi court was presented the question of whether the MPSC could regulate the rate at which the gas was being sold, first from the pipeliner to the retailer, and then ultimately to the retail customer. Under those circumstances, it was apparent that the MPSC could not limit the amount of gas purchased by the retailer because that was its only source: if it allowed the retailer to sell any amount of gas, it would have to be from the source whose price had been set by the FPC. The facts in *Nantahala* and *United Gas* of having only one source of power are in sharp contrast to the instant case where multiple sources and varying prices of power are available to MP&L.

In *Narragansett*, a Rhode Island utility sought increased rates for its retail customers based on the rates charged by its wholesaler, New England Power Company. The Public Utilities Commission of Rhode Island attempted to make a determination as to the reasonableness of the rates which New England Power Company was charging Narragansett. A determination by the state PUC of the reasonableness of the rates would duplicate the responsibilities of the FPC and thus unconstitutionally infringe. Relying on *United Gas Corp.* and the principal authorities applying the preemption doctrine in the field of interstate rate regulation, the Rhode Island Supreme Court reversed its Commission's effort to regulate the rates.

The *Narragansett* court stated, however, that the PUC was within its power to investigate the overall financial structure of the company to determine whether it had experienced savings in other areas which might offset the fuel adjustment clause. It concluded, "Therefore, we do not order the PUC to automatically adjust the retail rates in accordance with the purchase power cost adjustment clause." 381 A.2d at 1363.

The lesson from *Narragansett* is that the division of regulatory responsibilities between the federal and state governments should not leave gaps which are unregulated.[25] The states cannot establish rates for utilities' interstate sales nor can the federal government make rates for the retail customer. The prudence, or managerial wisdom, of MP&L's undertakings in connection with Grand Gulf is properly within the jurisdiction of the MPSC as it relates to a proposed retail rate increase. The investigation cannot legally conflict with the determination of FERC of MP&L's allocation of Grand Gulf capacity nor with the wholesale rates to be charged to MP&L for that power. The investigation by the MPSC, however, can and must lawfully be directed at the prudence of MP&L's undertakings with respect to Grand Gulf and the manner in which Grand Gulf expenses are to be recovered from MP&L's customers.

[25]That is not to suggest that to carry out those responsibilities is always a simple task. Dividing the costs of Grand Gulf will certainly impact on retail rates somewhere. The different obligations of the MPSC and the FERC are in whose interests are to be protected. The MPSC is concerned only with the MP&L retail ratepayers. The FERC was called on to divide the costs at Grand Gulf among operating companies. The FERC's attitude can be fairly read from a statement it made in a brief before the D.C. Circuit Court of Appeals: "But that [a substantial impact] is unavoidable; someone must pay for Grand Gulf."

The FERC's previous decisions have agreed with this position. See, *Philadelphia Electric Company*, 15 FERC ¶ 61,264 (1981);[26] *Pennsylvania Power & Light Company*, 23 FERC ¶ 61,325 (1983); *Southern Company Services*, 26 FERC ¶61,360 (1984).

Other states have been confronted with the regulation at retail of FERC approved purchases. In *Pike County Light & Power Company v. Pennsylvania Public Utility Commission*, 465 A.2d 735 (Pa. 1983), the FERC had approved an agreement for the purchase by a utility from its parent of wholesale power. In setting the utility's retail rates, the state Commission held that although it could not challenge the rates as being unreasonable, it could disallow purchase power expenses on the ground that more economical sources of supply were available. That court held:

> "The regulatory functions of the FERC and the PUC thus, do not overlap and there is nothing in the federal legislation which preempts the PUC's authority to determine the reasonableness of a utility's claimed expenses. In fact, we read the Federal Power Act to expressly preserve that important state authority."

Id. at 738.

This Court has recently recognized the nature of dual regulation in *Louisiana Public Service Commission v. Federal Communications Commission*, 476 U.S. 355 (1986). The issue was whether the state would be required to apply federally designed depreciation practices and charges as they related to the setting of intrastate telephone rates. The FCC had issued orders which proscribed the depreciation practices affecting telephone plant to be used in interstate commerce. The state adopted different depreciation

[26]Indeed in the cases involving the 1982 MSU filings, the intervening parties based their case strategies on this FERC decision on prudency.

practices. The problem arose when the different depreciation practices were applied to the same plant which was being used in interstate and intrastate service. Though the FCC claimed that its order preempted inconsistent state regulation, the Court recognized the limitation on the jurisdiction of the FCC with respect to intrastate communication service. 47 U.S.C. § 152(b).[27] This Court declined to disregard an express statement of congressional intent.

MP&L relies exclusively on *Nantahala* to frame the question it presents. *Nantahala* is self-distinguishing from this case and should not be relied upon for the proposition that FERC approved wholesale rates must be adopted as a federally imposed surcharge by the regulated retail rates regardless of all state requirements of ratemaking. A comparison of the facts in *Nantahala* with this case is useful.

Nantahala and Tapoco were both wholly owned subsidiaries of Alcoa. Both Nantahala and Tapoco transmitted all of their self-generated power to TVA. In return, through a series of FERC-approved agreements, Nantahala and Tapoco received from TVA a mix of low cost entitlement power while Nantahala bought an additional amount of the high cost purchase power from TVA. Any change in the mix of purchased power and entitlement power by Nantahala changed the cost of the power to both companies. 90 L.Ed.2d at 947. TVA was the only source of power available to Nantahala. *Id.* at 958. When the North Carolina Utilities Commission attempted to change the mix of entitlement power and purchased power, it necessarily changed the FERC allocated cost. This

[27]A provision very much in likeness to the jurisdictional restriction in the Federal Power Act, 16 U.S.C. § 824(a).

Court held that the action taken by the NCUC violated the Supremacy Clause.

The facts of this case are materially different. MP&L owns its own power located within its territorial jurisdiction as well as partial ownership in the Independence coal plants located in Arkansas. While MP&L is not a stand-alone company, since it operates through a system arrangement with its sister subsidiaries, its cost of energy and capacity are in direct relation to its own generation capacity.[28]

This Court's opinion in *Nantahala* spoke to the differences in that case from the set of facts which MP&L presents here, where the MPSC can consider the availability of sources of lower cost power even in the presence of a FERC-approved allocation. 90 L.Ed.2d at 958. This conclusion has been read to this effect by at least one circuit court of appeals. See, *New Orleans Public Service v. City of New Orleans*, 798 F.2d 858, 860 (5th Cir. 1986).[29] The Mississippi court reversed the action of the MPSC because it had adopted certain operating expenses in retail rates without any finding that they were just, reasonable and prudently incurred. In doing so, it did not act in derogation of the FERC or of its own recognition of the line between the interstate and intrastate ratemaking. This Court and the *Narragansett* doctrine are consistent in the view that "an increase in FERC-approved wholesale rates need not lead to an increase in retail rates." *Nantahala* at 955.

[28]The FERC decisions have in fact refused to equalize the investment costs of system-wide generation. *Middle South Energy, Inc.*, FERC Opinion 234, 31 FERC ¶ 61,305 (1985).

[29]This decision has added importance because the court was considering the impact of the same FERC order on New Orleans Public Service, Inc.

MP&L's argument with regard to the "trapping" of costs fails because of factual distinctions between *Nantahala* and this case.[30] Nantahala received all of its power through the FERC-approved arrangement from TVA. Any deviation from the arrangement produced a change in the price of the energy. A reduction in the *price* paid to Nantahala by its ratepayers resulted in a change in the *price* it had to pay its wholesale supplier. The cost differential was thus trapped. *Id.* at 956-7. But MP&L has sources of power other than Grand Gulf. Costs vary from each source. Changing the mix will not change the FERC ordered price of Grand Gulf generated energy but will only change the quantity of that energy used by MP&L. As plainly stated, this is not an impermissible exercise of the state's power to set retail rates. *Id.* at 958.[31]

[30]"Trapping" is a term of convenience used by MP&L in this case. " . . . MP&L admitted at oral argument that it is selling the less expensive energy off the system and retaining the electricity allocated to it from Grand Gulf." 506 So.2d at 985. Thus, MP&L has decided by which source of power it wants to be "trapped."

[31]Upon consideration on remand, if, for example, the MPSC were to find that because of the availability of sources of lower cost power to MP&L's retail customers, it would be reasonable for those consumers to take and pay for only one-half of that part of Grand Gulf owned by MP&L. MP&L would be free to dispose of the remaining amount of the wholesale purchase by its stockholders through sale to other utilities or to be absorbed by those stockholders as the wages of the competitive risks for the opportunity to make a profit. It is assumed that a profit to a regulated monopoly comes only with the exercise of a reasonable and prudent management. Were MP&L to be able to pass through the costs of its managerial imprudence, not only would the economic motive for good management evaporate, but the system of regulation would then be assuring a profit, contrary to settled law. See, for example, *Bluefield Waterworks & Improvements Co. v. Public Serv. Comm'n of W. Va.*, 262 U.S. 79, 692-93 (1923).

C. MP&L Should Be Equitably Estopped from Arguing to this Court That The Further State Action Required of the MPSC By The Mississippi Supreme Court is Preempted by Federal Law.

This Court should hold that prior representations and actions by MP&L and MSE to the MPSC to secure the necessary license from the State to construct the Grand Gulf plant and to add other new capacity equitably estop these affiliated utility companies from now claiming federal preemption of the further state actions mandated by the Mississippi court.

The doctrine of equitable estoppel is an ancient "... principal of law, older than the country itself ..." *Glus v. Brooklyn Eastern District Terminal*, 359 U.S. 231, 234 (1959). The doctrine stems from the maxim that no man should be allowed to take advantage of his own wrong. It has been stated in many forms by the courts of this nation using the same basic concept to deny requested relief in a variety of different legal actions.

Justice Miller expressed the doctrine in the following manner in *Union Mutual Insurance Co. of Maine v. Wilkinson*, 13 Wall 222, 233 (1872).

> The principle is that where one party has by his representations or his conduct induced the other party to a transaction to give him an advantage which it would be against equity and good conscience for him to assert, he would not in a court of justice be permitted to avail himself of that advantage. And although the cases to which this principle is to be applied are not as well defined as could be wished, the general doctrine is well understood and is applied by courts of law as well as equity where the technical advantage thus obtained is set up and relied on to defeat the ends of justice or establish a dishonest claim.

cf. Heckler v. Community Health Services, 467 U.S. 51, 59 (1984).

In the instant case, the State, through the MPSC, has relied to its detriment throughout the history of the Grand Gulf plant on the inaccurate representations of MP&L and MSE regarding how the capacity and energy of the plant would be allocated and the extent of state jurisdiction over Grand Gulf.

The initial representations made to the state are found in verified pleadings and sworn testimony by MP&L and MSE corporate executive officers which were made to the MPSC to gain the required certificate needed to construct the plant.[32] The Companies specifically acknowledged in 1974 that the construction and operation of Grand Gulf came within the "purview" of state law, specifically the Public Utilities Act of 1956, §§ 77-3-1, *et seq., Mississippi Code of 1972*. (Supp.App. at 25) Additionally, the companies set forth a specific methodology by which the MSU system would seek to allocate the capacity and energy of the plant. The MPSC subsequently accepted the representations of MP&L and MSE, incorporating them into the license itself. See, pp. 3, 4, *infra*.

Although it cannot be stated that the representations as to the manner in which the plant would be allocated were misrepresentations when originally made, they acquired that character when the operating companies of the MSU system began deliberations in 1977 to change the Grand Gulf allocation methodology. See *Middle South Energy, Inc.*, 26 FERC ¶ 63,044, at 65,101-65,103. These discussions and the various intrasystem allocation proposals were never revealed to the state even though radically different from the original representations.

---

[32] Congress has given the FERC no authority to license the construction of electric generating facilities even those planned exclusively for interstate use.

Even after the MSU operating companies finally settled on a different allocation methodology on July 10, 1980, almost a year passed before Mississippi officials became aware of the new MSU plan. At that time the information was not volunteered to the MPSC but rather a copy of the document signed by the presidents of the operating companies was acknowledged by MP&L's chief executive officer when confronted with it by an intervenor in a hearing before the MPSC. This occurred during a July, 1981 hearing on MP&L's request to purchase even more capacity from AP&L's Independence coal plant in Arkansas.

Further, during the same hearings, when the MP&L chief executive officer was questioned by state officials regarding the impact of the new allocation adopted by the MSU operating companies, he hastened to reassure them in unqualified terms that the MPSC had the jurisdiction and authority to make the ultimate determination as to the Grand Gulf costs which must be borne by Mississippi retail ratepayers. See pp. 4, 5, *infra*.

There can be little doubt that for a period of at least four years, MP&L officials engaged in a course of conduct concealing the actions of the MSU operating companies from Mississippi officials. Likewise, there can be no doubt that Mississippi has acted on such conduct and misrepresentations to its detriment. The MPSC granted the necessary license to construct the Grand Gulf Plant in spite of its huge projected construction costs secure that the representations made to it in verified pleadings and sworn testimony about how the MSU system would seek to allocate the plant would be followed. Even after the secret intrasystem agreements were involuntarily disclosed and acknowledged, the MP&L chief executive officer defused the disclosure by reaffirming the jurisdictional authority

of the state over the plant. Thus, during the period from 1977 until 1982 when MSE sought approval of the allocation of the plant from FERC, a period in which nuclear plant construction costs soared and electric demand plummeted, the misrepresentations and actions of MP&L and MSE officials caused the State to sleep on whatever lawful actions[33] it may have taken to alleviate the tremendous cost burdens subsequently imposed on Mississippi ratepayers. Indeed, the MPSC even authorized MP&L to acquire additional capacity from the ISES plants in Arkansas.

This Court has applied the doctrine previously in an instance in which a party has utilized state laws to its advantage and then later complained about their effect. In *William E. Wall v. Parrot Silver & Copper Company*, 244 U.S. 407 (1917), the appellants claimed state law requirements resulted in the taking of their property thus violating the "due process of law" and the "equal protection of the laws" clauses of the Fourteenth Amendment. The Court upon examination of the case record agreed with the holding of the lower court that appellants had failed to sustain their original allegations; however, the Court stated its preference for application of equitable principles. The Court stated:

> This record does not call upon us to examine into this challenge of the validity of these statutory provisions, similar as they are to those of many states and of a seemingly equitable character, for the reason that the appellants, by their actions . . . pursuant to these statutes . . . waived their right to assail the validity of them. [Citations of authority omitted].

---

[33]One possibility during the early stages of the plants construction was cancellation of the license to build the plant. MP&L and MSE apparently acknowledged such state authority since a 1986 MPSC order revoking the license to construct the second unit of Grand Gulf was not appealed.

> They cannot claim the benefit of statutes and afterward assail their validity. There is no sanctity in such a claim of constitutional right as prevents it being waived as any other claim of right may be.

Id. at 411. *See also Exchange Trust Co. v. Drainage Dist. No. 7*, 278 U.S. 421, 425 (1929) in which the Court refused to allow an appellant to attack the validity of an administrative agency actions after it had received the benefits. Cf. *Federal Power Com'n v. Colo. Interstate Gas Co.*, 348 U.S. 492, 502 (1955).

MP&L seemingly argues that the application of the doctrine is inappropriate in this case because:

> " . . . FERC rejected this argument on the ground that the Mississippi PSC certificate was not conditional on any particular allocation method and that the Mississippi PSC did not in any event, have the authority to prescribe any allocation of wholesale costs and capacity among system companies. . . .

Appellants' Brief at 13. Contrary to this argument, examination of the certificate reveals an expectation that the MSU system would act as its officials testified and make application to FERC for the allocation methodology described in the certificate. Further, application of the doctrine would not "prescribe" any allocation of wholesale costs and capacity among system companies, rather it would act only to preclude an unjust result upon Mississippi retail ratepayers.

An additional argument advanced by FERC and embraced by the Court of Appeals for the District of Columbia Circuit (808 F.2d at 1549-50), was that the FERC could not be bound by such representations in any event because FERC " . . . made no representations to MPSC, its hands could not be tied by the doctrine." These two tribunals misperceived the thrust of the estoppel doctrine. The doctrine negates the standing of an individual or

other party to obtain relief because of prior acts *not* the ability of the tribunal to grant or deny relief. This appellee asserts that the federal bodies should have applied the doctrine and should have denied standing to the MSU System to file an application with FERC, or enforce any allocation against the Mississippi service area other than originally represented to secure the necessary construction certificate.

It is important to note that the representations made to the MPSC were a component of the Mississippi court's decision. That court referred to the representations in the original MPSC order as reflecting " . . . the understanding of all of the parties involved . . ." (506 So.2d at 980; J.S. App. 5a)

Further, it should be noted that equitable estoppel was applied to SERI for these same representations when that company requested the U. S. District Court for the Southern District of Mississippi to deny the MPSC access to its records for the purpose of conducting a financial audit. That court stated:

> This Court is persuaded that the equitable estoppel argument is tenable in this case. Since SERI subjected itself to state regulatory authority in order to obtain its certificate, it cannot now claim that it was never subject to that authority.

(Supp. App. at 46) Consequently, the court held that SERI was bound by its representations in 1974 that it came under the purview of the Mississippi Public Utility Act of 1956 and that court required SERI to disclose its financial records to the MPSC for a financial audit.

D. The Mississippi Decision Did Not Violate The Commerce Clause.

No rates have yet been set by the MPSC so that any determination can be made with regard to the effect on interstate commerce. There can be no doubt that the MPSC can proceed with its retail ratemaking responsibilities by determining from the available sources of power the most prudent and economical mix for the ratepayers in the MP&L jurisdiction. Sources of power before the MPSC will include MP&L's native load located in Mississippi, its interest in the ISES in Arkansas, as well as the power from Grand Gulf which is located in Mississippi.

There is no Mississippi statute being applied which requires the embargo for Mississippi consumers of lower costs energy, action prohibited in *New England Power Company v. New Hampshire*, 455 U.S. 331 (1982). Nor is there any evidence that any decision which the MPSC could make would directly or indirectly affect out-of-state economic interests. *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, — U.S. —, 106 S.Ct. 2080 (1986).

To speculate at this point that a decision of the MPSC to pass to its consumers any amount of the cost of Grand Gulf less than 33% would impose a prohibited burden on interstate commerce would be to foreclose almost all state electric utility regulation. Any state ratemaking action will have some influence or some effect upon interstate commerce but these actions are not necessarily prohibited. *Arkansas Electric Coop Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 395 (1983). Contrary to the assertion of MP&L, *Nantahala* contemplates that the role of the intrastate ratemaking agency will be selective among sources of power.

MP&L attempts to raise to the level of a Commerce Clause violation the possibility that the MPSC will conclude that MP&L has sufficient lower cost native load power available to serve its customers without some or all of the Grand Gulf power.[34] What MP&L characterizes as offensive of the Commerce Clause, if advocated by Mississippi, is apparently contemplated itself in the 1982 System Agreement approved by the FERC. Article IV, § 4.01 states: "Each Company shall normally own, or have available to it under contract, such generating capability and other facilities as are necessary to supply all of the requirements of its own customers." The claims of MP&L that a decision of the MPSC to adopt as retail rates any percentage of Grand Gulf less than the total 33% would result in a *per se* violation seems highly unlikely in view of the fact that AP&L, LP&L, and NOPSI have agreed with their state commissions to charge their customers substantially less than the amounts allocated to them. See pp. 15 and 16, *infra*. It is submitted that if the actions of these states' public service commissioners are not *per se* violations of the Commerce Clause, MP&L is hard pressed to claim some potential act by the MPSC is a violation.

Should the decision of the Mississippi court fail to constitute a *per se* violation of the Commerce Clause, MP&L urges the Court to find that the decisions fails the balancing test of *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970). To so hold requires the Court to determine wheth-

---

[34]Brief of Appellant, p. 44. Again, appellant characterizes this as "Mississippi's challenge." It must be repeated that the Mississippi court did not challenge anything but it simply remanded the decision of the MPSC to the administrative agency to fulfill its duties. To this point, there has been no "challenge" by Mississippi but rather it is MP&L that seeks an advisory opinion from this Court in the event some challenge to that effect is made.

er there are local benefits that can justify the burden on commerce. Appellant makes no mention of any local benefits which might flow from local ratemaking by the MPSC concluding that "[a]ll Mississippi's legitimate interests are being fully protected by FERC." Brief of Appellant, p. 45. Such a statement ignores the omission of prudency considerations by the FERC; ignores the intent of Congress to reserve those responsibilities to the states; ignores the history of the FERC in investigating prudency matters; ignores the flat statement by the MPSC that it did not consider matters of prudency, excess capacity or other gravely important considerations.

This appellee doubts that the framers of our Constitution would recognize the type of commerce now alleged as being burdened by Mississippi. Far from the uncomplicated interstate transactions occurring in our nation in the 1780's, the "commerce" involved in this case is more than just a commodity for sale since it is also an allocation of the investment costs for manufacturing the product among affiliated subsidiaries of a huge public utility holding company. The arguments of Appellant and Amici seek to elevate the importance of such financial intercorporate transactions above the regulatory interests of a state. To do so would raise the constitutional status of such corporation above one of the legitimate partners to the federal compact. We contend that the Constitution has never sanctioned such action and Congress, at least in terms of the Federal Power Act, did not enact such expansive legislation.

E. To deny the MPSC the Jurisdiction to Proceed With Establishing Retail Rates in Mississippi Would be Contrary to Important Public Policy.

This controversy arises from the exercise by the FERC of jurisdiction over Grand Gulf. A reversal of

the Mississippi Court's decision relying on the validity of that exercise of jurisdiction would indeed be on unsure ground. The FPA expressly prohibits the jurisdiction of the FERC, "over facilities used for the generation of electric energy. . . ." 16 U.S.C. § 824(b)(1) (1982). The Court has read that statutory language as it is written:

> It is hard for us to believe that Congress meant us to read "shall have jurisdiction" where it had carefully written "but shall not have jurisdiction." The command "thou shalt not" is usually rendered as to forbid and we think here it was employed without subtlety or contortion and in its usual sense.

Connecticut Light & Power Co. v. FPC, 324 U.S. 515, 528-29 (1945). It is likely that this issue will be presented to the Court when *Mississippi Industries* comes to this Court for review.[35]

It is the states which have the authority to certificate electric generation facilities and they are in the best position to evaluate the immediate and long-range needs of their constituents. *Pacific Gas, supra*. The state regulatory agencies have as much incentive to cooperate with others as the FERC—perhaps more. The participation of the MPSC in the Grand Gulf construction is a case in point. The MPSC approved the certificate for the Grand Gulf construction, knowing that it was for the benefit of the system as a whole, yet acting to protect (or so it appeared) the interests of the Mississippi retail ratepayers. At that time, the MPSC relied on the representations that MP&L would be responsible for about 19% of

---

[35]Arkansas parties presented this question in a petition for a writ of certiorari *sub nom, Arkansas Public Service Commission, et al. v. FERC*, Nos. 86-1424, 86-1380, and 87-469. Cert was denied on December 14, 1987. This question likely will be preserved and presented to the Court when the entire *Mississippi Industries* case has been finally reviewed by the District of Columbia Circuit.

Grand Gulf. Thus, the MPSC cooperated with the stated intentions of the MSU system as a full partner.

Not only does the action of the FERC in asserting jurisdiction over Grand Gulf violate the federal law, its effect is to create a regulatory gap which will lead to the very confusion and disruption of efficient and economical delivery of electric power that the FPA was intended to cure. That occurs in two ways. First, to accept the position of appellant, Mississippi consumers will be forced to accept the result of the decision of MP&L's management without any review of its prudency or reasonableness. It has already been established that there has been no such review at any level.

Secondly, the FERC is in an untenable position to adequately conduct prudency reviews which consider the local conditions existing in each territory served by an electric utility which would be subject to the FERC jurisdiction. How would it measure the needs of the Mississippi, Louisiana or New Orleans ratepayers? Would it compare or contrast the diverse needs of the city occupants of New Orleans or the rural, residents of the Mississippi Delta? Could it insure that the affected citizens could afford the decisions it makes? Would it conduct hearings in Mississippi or Louisiana or would it force those individual citizens to come to Washington for its hearings. Without substantial congressional assistance and appropriation, the FERC cannot reasonably claim to be prepared to absorb the important duties now fulfilled by the state utility regulatory agencies.

A major, dramatic impact of a reversal of the Mississippi court's decision would be the chilling impact it would have on the willingness of states to certify large system-wide generating plants. Clearly, if the various state commissions were unable to rely on the sworn representations

made to secure the all important construction license for such generating plants, what commission would be foolish enough to authorize new plants? Thus, the very efficiencies and economies sought by the FERC and Congress through adoption of the FPA would be defeated.

CONCLUSION

For the reasons stated in this brief and the motion to dismiss, Appellee, State of Mississippi respectfully requests this Court to dismiss the appeal of the decision of the Mississippi Supreme Court by Appellant, MP&L; or should the Court acknowledge jurisdiction of this cause, to affirm the decision of that Mississippi Supreme Court.

DATED: January 22, 1988

Respectfully submitted,

State of Mississippi
Mike Moore
Attorney General

Frank Spencer
Assistant Attorney General
W. Glenn Watts
Special Assistant
Attorney General
P.O. Box 220
Jackson, Mississippi 39205
(601) 359-3680

*John L. Maxey, II
Cupit & Maxey
304 North Congress St.
P.O. Box 22666
Jackson, Mississippi 39205
(601) 355-1553

Attorneys for Appellee State of Mississippi

* *Counsel of Record*

REPLY BRIEF

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

APPELLANT'S REPLY BRIEF

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi
39205
(601) 354-2385

Of Counsel:
WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 298-1800

Attorneys for Appellant

Counsel of Record

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN,
Attorney General, and THE
MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court
of Mississippi

APPELLANT'S REPLY BRIEF[1]

I. Mississippi's Actions Violate The Federal Power Act And The Commerce Clause.

The arguments of the State of Mississippi and its *amici* reduce to a single contention: that the rule of *Nantahala Power & Light Co.* v. *Thornburg*, and its precursors, improperly derogates from the states' authority to set retail electric rates.[2] This is simply incorrect. *Nantahala* has no effect on any legitimate state interest.

Under *Nantahala*, state ratemaking authority is preempted in only one limited respect. The state commission is required to

[1]The Statement required by Rule 28.1 appears at page ii of Appellant's Brief.

[2]For example, Mississippi states (p. 1) that MP&L and FERC are contending that FERC's regulation has "preempted the jurisdiction of the State of Mississippi to set retail electricity rates" and would deprive states of "responsibility for the setting of retail electricity rates."

include in the local utility's retail revenue requirements those purchased power expenses which FERC has determined to be "just and reasonable." Under *Nantahala*, the state commission retains plenary authority to determine all other components of retail revenue requirements: from the retail rate base, to the rate of return, to other operating expenses.[3] The state commission further retains the authority to design the specific rates under which the utility may recover its revenue requirements and to determine the manner and time frame in which extraordinary expenses will be recovered.

The point is illustrated by the retail rate order that FERC and MP&L are *defending*. The Mississippi PSC here recognized MP&L's FERC-mandated Grand Gulf 1 expenses. It decided to phase-in their recovery over 10 years and to spread the collection of deferred amounts over 40 years. It determined all other elements of MP&L's retail revenue requirements, allowing MP&L $46 million less than it originally requested. *See* Final Order, p. 18 (June 14, 1985) (R. 2147). The Mississippi PSC then set the specific retail rates that allocate MP&L's overall revenue requirements among its different classes of residential and business customers.[4]

[3]In this respect, the contrast between this case and *Louisiana Public Service Comm'n* v. *FCC*, 106 S. Ct. 1890 (1986), could not be more stark. Unlike the Federal Power Act, the Communications Act contains a provision (47 U.S.C. § 152(b)) that preserves exclusive state jurisdiction over all aspects of the establishment of rates for intrastate telephone service. There, the FCC and the Court of Appeals had nonetheless held that FCC regulations could prescribe depreciation rates and any other elements of intrastate ratemaking that affect the financial strength of telephone companies that also provide interstate services. The Court rejected this position. Even then, the Court made it explicit that it was not disturbing the FCC's authority to preempt state jurisdiction over intrastate services when essential to the FCC's regulation of interstate services. 106 S. Ct. at 1902 n.4.

[4]Mississippi's Brief misstates the effect of the Grand Gulf 1 expenses on MP&L's rate levels. The table reprinted on page 7 of that brief shows

(Footnote continued on next page)

While *Nantahala* does not substantially interfere with state jurisdiction over retail rates, it is essential to the implementation of the Federal Power Act. The facts of this case illustrate the point.

It is undisputed that the Middle South System is an integrated system with diversified fuel sources, that MP&L and other MSU companies acquire generation for the benefit of the system ratepayers as a whole, and that FERC regulation allocates the high-cost and low-cost power to roughly equalize the generation costs of MP&L and each other MSU operating company. Similarly, no one disputes that FERC Opinions 234 and 234-A both (1) established "just and reasonable" wholesale rates for MSE's sales of the output of Grand Gulf 1 and (2) held that it is "just and reasonable"—indeed required by the Federal Power Act[5] —for MP&L to purchase 33% of Grand Gulf 1's output and thus to use correspondingly less of the lower-cost power of MP&L and other MSU operating companies. In making this determination, FERC applied the *same* basic principles of utility regulation that

(Footnote continued from previous page)

projected increases in MP&L's customers' bills over a five-year period from all sources, not just from the inclusion of Grand Gulf 1 expenses. These increases are in line with those that other electric utilities are experiencing.

In this regard, Mississippi's assertion (pp. 7–8 & n.9) that MP&L's rates are higher than 70% of the utilities in the country is incorrect. Mississippi's assertions are based on statistics that rank the average bills of customers with 500 kwh of monthly consumption. However, it is undisputed that the average MP&L residential customer consumes 1000 kwh per month (*see* R. Notice Vol. 2, p. 14; Ex. 47, schedules 5, 7, 17, & 18), that MP&L's retail rates are designed to minimize the impact on the average residential customer, and that MP&L's average residential customer has lower bills than the national average. *See* Appellant's Br., p. 19 n.19.

[5]FERC and the District of Columbia Circuit so held in rejecting the contentions of the Mississippi Attorney General, the Mississippi PSC, and other Mississippi parties. They had urged that MP&L be allocated either none of the Grand Gulf 1 capacity, or substantially less than 33%. FERC and the District of Columbia Circuit each considered this contention and held that it would be "unjust, unreasonable, and discriminatory" and a violation of Section 205 of the Federal Power Act. *See* Appellant's Br., p. 12.

state commissions employ[6]—except FERC does so free of the parochialism that can inevitably influence cost-allocation decisions of individual states. That is why FERC was created.

Thus, if the Mississippi PSC could set retail rates by redetermining the appropriate "mix" of MP&L's high-cost and low-cost power sources, it would nullify FERC's decision for the only purpose for which it matters in an integrated system: the recovery of these expenses from the ultimate consumer. No one disputes that the result would be that MP&L would suffer over $600 million in "trapped costs," contrary to *Nantahala*.[7] *Compare* Appellant's Br., p. 30 n.27.

The attempts of Mississippi and its *amici* to defend the Mississippi Supreme Court's judgment underscore the assault on FERC's regulation and on *Nantahala*. They are seeking to redetermine one of two matters, both of which are within FERC's exclusive jurisdiction: (1) the reasonableness of MP&L's allocation of 33% of Grand Gulf 1's capacity and (2) the reasonableness of the Middle South System's decision to construct and complete Grand Gulf 1.

[6]In this respect, the arguments that the MSU System has avoided regulation cannot be sustained. Not even the appellees or their *amici* suggest that FERC regulation is not just as stringent as that of any state. Beyond that, the Middle South System is subject to additional regulation by the SEC under the Public Utility Holding Company Act of 1935, which rests on the Congressional finding that affiliate power transactions within such multistate systems "are not susceptible of effective control by any State." 15 U.S.C. § 79a(a). The SEC has determined that it is in the public interest for the MSU companies to operate "as a single interconnected and coordinated system," rather than as five separate companies. *Middle South Utilities*, 35 SEC 1 (1953); *see* 15 U.S.C. §§ 79b(a)(2).

[7]Two separate courts of appeals have decided cases involving other MSU companies (AP&L and NOPSI), and each court has reached the obvious conclusion that *Nantahala* requires retail ratemaking authorities to include FERC-mandated Grand Gulf 1 expenses in retail revenue requirements. *Arkansas Power & Light Co.* v. *Missouri Public Service Comm'n*, 829 F.2d 1444, 1451 (8th Cir. 1987); *New Orleans Public Service, Inc.* v. *City of New Orleans*, 833 F.2d 583, 586 (5th Cir. 1987).

A. Mississippi Is Preempted From Redetermining The Optimal "Mix" Of MP&L's High-Cost Grand Gulf 1 Power And Other Lower-Cost Generation.

Mississippi's Brief candidly states (p. 44) what the Mississippi PSC would do on remand; it would exercise its "retail ratemaking responsibilities by determining from the available sources of power the most prudent and economical mix for the ratepayers in the MP&L jurisdiction." Specifically, Mississippi states (p. 44) that the Mississippi PSC would examine all the "[s]ources of power" that are available to MP&L, including its "native load located in Mississippi, its interest in the ISES in Arkansas, as well as the power from Grand Gulf." *See* Br., p. 36.[8] Mississippi states (p. 37 n.31) that the MPSC would disallow some or all of MP&L's FERC-mandated Grand Gulf 1 expenses if it found that MP&L had "sources of lower cost power [than Grand Gulf]." Mississippi argues (p. 37) that this result is not inconsistent with the Federal Power Act because "[c]hanging the mix [of high-cost and low-cost energy] will not change the FERC ordered price of Grand Gulf generated energy but will only change the quantity of that energy used by MP&L."

This is an assault on FERC's regulation, on *Nantahala*, and on common sense. Mississippi is arguing that the Mississippi PSC should do precisely what FERC has already done. All the power

[8]Mississippi (p. 3) refers to the fact that the Middle South System occasionally makes spot purchases of energy from nonaffiliated utilities. The system's dispatcher does so when another utility offers to sell the energy at a price that is below the variable costs (*e.g.*, fuel and labor) of generating those kilowatt-hours of energy from the facilities of MP&L or other MSU companies. These energy purchases are irrelevant to this case, which involves long-term *capacity* requirements—the ability to generate sufficient kilowatts to meet customer demand at any one time.

A utility's capacity requirements can only be satisfied either by the ownership of generating facilities or by firm long-term contracts to purchase the output of particular facilities. *See* Appellant's Br., p. 5 n.4. FERC has found that it was reasonable for the Middle South System to build Grand Gulf 1 to meet its capacity requirements. *See* Appellant's Br., pp. 13-14 & n.13.

sources of MP&L and the Middle South System were before FERC in Opinions 234 and 234-A. FERC then held that the Federal Power Act requires that MP&L purchase 33% of the Grand Gulf 1 output, and FERC rejected proposed allocations under which MP&L would use more lower-cost power instead. To set retail rates as if MP&L received a lesser, or zero, Grand Gulf 1 allocation would nullify this FERC determination. Indeed, each aspect of MP&L's power supply arrangements of which Mississippi's Brief complains is dictated by the two FERC rate schedules that FERC prescribed in Opinions 234 and 234-A.[9]

[9]For example, Mississippi objects (pp. 12-13) to the fact that over 1100 megawatts of MP&L-owned capacity have been "sold off" to other MSU companies each month "not at the cost of production, but at the price of the older oil and gas capacity costs." But the equalization payments to which Mississippi is referring are requirements of the rate schedule that FERC approved (the 1982 System Agreement). *See* Appellant's Br., pp. 10-11 & n.12, p. 17 n.16. Mississippi's assertion (p. 37 n.30) that MP&L made an independent decision to make these "sales" of capacity is simply false.

Similarly, Mississippi's repeated assertions (*e.g.*, p. 2) that the "total MP&L capacity" exceeded its customer needs by 76% before Grand Gulf 1 went on line are meaningless in view of the FERC rate schedules. MP&L is not a stand-alone company. It is part of an integrated system in which each company acquires capacity to meet the needs of the Middle South System as a whole and in which the companies sell and exchange electricity. The FERC rate schedules *require* that other MSU companies make equalization payments to MP&L for all its capacity in excess of MP&L's pro rata share of the capacity of the entire MSU System (which includes a system-wide reserve margin). *See* Appellant's Br., p. 11 n.12. The MSU System's capacity reserve margin reflects the reality that every utility must have sufficient capacity to meet its peak demand, plus a reasonable reserve. *See* Appellant's Br., p. 5 n.4. The record shows that MP&L's customers support a capacity "reserve" margin of 24%. R. 2945-47.

Finally, the amount of MSU's capacity reserve margin is unaffected by the amount of MP&L's Grand Gulf 1 allocation; MSU has the same amount of capacity whether MP&L's allocation is 0% or 33%. Thus, Mississippi's claims of "excess capacity" were irrelevant to its arguments in the Mississippi Supreme Court and are irrelevant here.

Mississippi and its *amici* offer an array of arguments why *Nantahala* permits state regulatory commissions to set retail rates as if the local utility receives a different mix of low-cost and high-cost power than FERC has ordered. Each is contradicted by *Nantahala*.[10]

Mississippi's principal claim is that North Carolina's actions in *Nantahala* were held to be preempted because a "reduction in the *price* paid to Nantahala by its ratepayers resulted in a change in the *price* it had to pay its wholesale supplier." Br., p. 37 (emphasis in original). This is simply incorrect. In *Nantahala*, North Carolina's actions had no effect on the price Nantahala paid. To the contrary, Nantahala continued to incur the purchased power expenses that resulted from the FERC rate schedules after North Carolina prohibited Nantahala from recovering those expenses in its retail rates. That is why this Court held that North Carolina's action produced a prohibited "'trapping' of [FERC-mandated] costs." *Nantahala*, slip op. at 17; 106 S. Ct. at 2359. Mississippi's proposed disallowance of MP&L's Grand Gulf 1 expenses would produce the same prohibited trapping of cost. *See* Appellant's Br., pp. 38–39.

Similarly, Mississippi asserts (p. 36) that *Nantahala* permits states to disallow FERC-mandated costs "even in the presence of a FERC-approved allocation" if there are "sources of lower cost power" and that the Court approved the so-called *Pike County* rule in this circumstance.[11] Again, *Nantahala* held precisely the

[10]For example, the *amicus curiae* brief of the National Governors' Association, *et al.*, admits (pp. 16–17) that *Nantahala* applies to the "purchased power component of the retail rate," but states erroneously that MP&L's Grand Gulf 1 expenses are part of a "capital cost component." Because Grand Gulf 1 expenses are "purchased power expenses," the National Governors' Association's own argument establishes that Mississippi's actions are preempted.

[11]*See Pike County Light & Power Co.* v. *Pennsylvania Public Utility Comm'n*, 77 Pa. Commw. 268, 465 A.2d 735 (1983); *Appeal of Sinclair Machine Products, Inc.*, 126 N.H. 822, 498 A.2d 696 (1985). A recent case following *Pike County* is *Kentucky West Virginia Gas Co.* v. *Pennsylvania Public Utility Comm'n*, No. 87-3052 (3d Cir. Jan. 19, 1988). This decision emphasizes that *Pike County* can apply only when FERC's regulation determines whether a "seller is charging a just and

(Footnote continued on following page)

opposite. It held that when, as here, FERC has effectively fixed the relative amounts of low-cost and high-cost power that a utility must purchase, a state commission must treat the resulting costs as "a reasonably incurred operating expense" and may not set retail rates as if the local utility used more low-cost power than FERC has allocated.[12] *See* Appellant's Br., pp. 40–41. Compliance with a FERC allocation order cannot be "imprudent."[13]

(Footnote continued from previous page)
reasonable wholesale rate based upon its cost of service," but "does *not* take the further step" and determine whether the retailer's purchase of a particular quantity of power at a particular price is "just and reasonable" to the "retail" utility. Slip op. at 18, 20 (emphasis added).

Here, in contrast, FERC made the latter determination—as FERC must do in cases involving an integrated interstate system like Middle South's. In such systems, the affiliated "retail" utilities each acquire generation, pool it, and exchange electricity with one another. Thus, each "retail" utility is also a "wholesale" utility, and FERC alone has jurisdiction to assure the fairness of the pooling arrangements to each utility and its customers. *Compare Kentucky Power Co.*, 38 FERC (CCH) ¶ 61,243, at 61,822-24 (1987), *with Philadelphia Electric Co.*, 15 FERC (CCH) ¶ 61,264 (1981).

[12]Moreover, in contrast to *Nantahala*, there is no basis for the state even to inquire into whether MP&L has alternative power sources. That inquiry was made in *Nantahala* because FERC allocated the low-cost TVA entitlements power, but had not ordered Nantahala to obtain any particular quantity of high-cost TVA purchased power. Thus, it was appropriate to inquire whether Nantahala had lower-cost alternatives to the high-cost TVA purchased-power—as this Court held it did not. *Nantahala*, slip op. at 19, 106 S. Ct. at 2360.

Here, in contrast, FERC has ordered MP&L to buy 33% of Grand Gulf 1's high-cost output, and rejected proposed allocations in which MP&L would rely on lower-cost power instead. Under FERC's order, it is irrelevant whether there are lower-cost alternatives to Grand Gulf 1; MP&L must buy 33% of Grand Gulf 1's output in any event.

[13]Similarly unavailing—and erroneous in fact—is Mississippi's assertion (p. 37) that FERC has fixed only the price which MP&L must pay for Grand Gulf 1 power, but has not allocated the quantity. The principal issue that FERC decided was how much of Grand Gulf 1's capacity should be allocated to each of the MSU companies.

Finally, Mississippi (p. 36) relies on the fact that *Nantahala* recognized that "an increase in FERC-approved wholesale rates need not lead to an increase in retail rates" because the state utility commission may find that there have been offsetting savings in the other aspects of the local utility's business. This argument, too, is baseless. In this retail rate case, the Mississippi PSC determined *all* MP&L expenses and revenue requirements—non-Grand Gulf 1 as well as Grand Gulf 1—and the MPSC established retail rates that reflected all the savings that MP&L enjoyed in the other aspects of its business. *See* Appellant's Br., pp. 17–18 & n.17. Thus, there was only one ground on which the Mississippi Supreme Court could, and did, reverse this rate order: that it was error for the Mississippi PSC to include MP&L's FERC-mandated Grand Gulf 1 expense in retail revenue requirements without first making an independent determination of the "prudency" of MP&L's 33% allocation. This is precisely what *Nantahala* held to be prohibited by federal law.

B. States Are Equally Preempted From Determining The Prudence Of MSE's And The Middle South System's Decision To Construct And Complete Grand Gulf 1.

It is clear that FERC has allocated all the power on the Middle South System; it required MP&L to purchase 33% of Grand Gulf 1 and rejected allocations in which MP&L would rely on lower-cost power sources instead. As Mississippi's *amici* recognize, these facts establish that MP&L has no "freedom of action" in its Grand Gulf 1 purchase and foreclose any argument that MP&L is acting "imprudently" today. *See* Consumer Federation of America Br., p. 12. Mississippi's *amici* thus defend the Mississippi Supreme Court's judgment on a different ground. They claim that the real issue is whether MP&L, MSE, and Middle South were guilty of "imprudent management" between 1974 and 1982 in deciding to build and complete Grand

Gulf 1. Mississippi and its *amici* alike argue that *Nantahala* permits states to determine the prudence of such power supply decisions and that, in any event, FERC neither could make, nor did make, this determination.

Preliminarily, there is no substance to the contentions that *Nantahala* did not involve claims of "imprudent management" and that its holding is limited to questions involving the allocation of costs that were prudently incurred. *See* New Orleans Br., p. 21; Consumer Federation of America Br., p. 5. The fundamental issue that gave rise to the *Nantahala* litigation was whether (as infallible hindsight suggested) Nantahala had not acted in the best interests of its customers in 1963, when Nantahala entered into a 20-year agreement (the New Fontana Agreement ("NFA")) to transfer the entire output of its generating facilities to TVA in exchange for fixed entitlements of TVA power. North Carolina found that this decision had been made to benefit Nantahala's shareholder (Alcoa) rather than its customers, and was therefore imprudent. North Carolina thus proceeded to set retail rates as if the NFA had never been entered into at all. This order was held preempted by the Federal Power Act because FERC had found that the NFA was fair to Nantahala's public service customers and had modified the separate Apportionment Agreement to prescribe a different interstate cost allocation than North Carolina's. *Nantahala*, slip op. at 15, 106 S. Ct. at 2358. In short, it was FERC's jurisdiction to assure that Nantahala's wholesale transactions with TVA were "just and reasonable" that preempted the North Carolina retail rate order.

Nevertheless, Mississippi and its *amici* argue that FERC has not, and could not, determine whether the Middle South System behaved prudently in planning, constructing, and completing Grand Gulf 1. They claim that there will be a "regulatory gap" unless *each* of the five regulatory bodies that regulate the retail rates of Middle South companies can independently determine

this matter and then exclude from retail rates any Grand Gulf 1-related expenditures that are deemed to have been imprudent. That would mean that MSE would effectively have a different wholesale rate base in each of the five MSU jurisdictions. These contentions are baseless.[14]

FERC has exclusive jurisdiction to set the "just and reasonable" rates for MSE's wholesale sales of the power generated by Grand Gulf 1. The establishment of "just and reasonable" rates is, by definition, a determination that the utility's underlying expenses and investment were prudently incurred. Thus, inherent in any establishment of just and reasonable rates for Grand Gulf 1 is a determination of whether and to what extent it had been prudent for MSE to plan, construct, and complete Grand Gulf 1—in view of any alternative power supply sources that then existed. In fact, FERC has repeatedly held that it will exclude from a utility's wholesale rate base any investments that were imprudently incurred.[15]

---

[14]Spreading the authority to make these determinations over the five retail ratemaking authorities would completely thwart the Federal Power Act's requirement of just, reasonable, and non-discriminatory rates. In this case, for example, the MPSC would presumably give Mississippi the same Grand Gulf 1 allocation that it advocated so vigorously before FERC—very little in the early years when costs are high, and more in later years when costs are lower. The Arkansas Public Service Commission would certainly assign to its ratepayers the same 0% allocation for which it has litigated in several forums, and the allocations by the Louisiana Public Service Commission and the City Council of the City of New Orleans would similarly favor their own ratepayers.

The combined results of these separate proceedings would be the complete disintegration of FERC's considered decisions that (1) Grand Gulf 1 was a system undertaking whose costs must be shared among all operating companies and (2) the allocation which would result in just and reasonable rates was the allocation which FERC ordered.

[15]*See, e.g.*, *New England Power Co.*, Opinion No. 295, Docket ER 85-646 (Jan. 15, 1988); *Union Electric Co.*, 40 FERC (CCH) ¶ 61,046 (1987); *New England Power Co.*, 31 FERC (CCH) ¶ 61,047 (1985); *Arizona Public Service Co.*, 27 FERC (CCH) ¶ 61,185 (1983).

Thus, if the issue of the prudence of MSE's decision to construct and complete Grand Gulf 1 were still open, it manifestly may not be litigated before the Mississippi PSC. The exclusive remedy of Mississippi and its *amici* is to file a complaint before FERC under Section 206 of the Federal Power Act and seek to modify MSE's Grand Gulf 1 rates on the ground that some of the underlying investment was imprudently incurred.

However, the issue is not open. The sole basis for the contrary assertions of Mississippi and its *amici* is the statements that one of the two FERC Administrative Law Judges assigned to this matter made at a pretrial conference. But these statements are quoted out of context. What the ALJ stated is that he "would not get into a prudency argument *unless one of the Intervenors raises a prudency question*." Miss. Supp. App., p. 61 (emphasis added); *see also id.*, pp. 60–64. The ALJ's statements simply reflected FERC's long-established practice of presuming the prudence of a wholesale utility's investment and costs unless an intervenor makes a contrary claim—as no intervenor had yet done in these FERC dockets. *See* Appellant's Br., pp. 13–14 n.13.

More fundamentally, it is undisputed that MSE had introduced extensive evidence that the construction and completion of Grand Gulf 1 was prudent in view of the other existing power sources. FERC explicitly so found. *See* Appellant's Br., pp. 13–14 n.13. Thus, wholesale rates were established that permit MSE to earn a return on 100% of its Grand Gulf 1 investments. *Id.* If the Mississippi parties and their *amici* thought that these findings were procedurally or substantively improper (*compare* New Orleans Br., p. 18 n.15), their exclusive remedy was to challenge the findings on appeal.

In all events, they cannot litigate the issue before a state commission now. The Mississippi Attorney General may not make a strategic decision to decline to litigate prudence claims that are within FERC's exclusive jurisdiction before FERC and

then seek to raise those issues in state forums on the theory that FERC has not decided them. The whole purpose of the Federal Power Act was to centralize these determinations in a single, neutral federal forum. If the issue is open, Mississippi and its *amici* should return to FERC.

C. The Generating Facility Licensing And Equitable Estoppel Arguments Are Meritless.

Finally, Mississippi and its *amici* seek to challenge FERC's authority to issue Opinions 234 and 234-A, on two separate grounds. Each claim is foreclosed by *res judicata* and Section 313 of the Federal Power Act. Each claim is also spurious.

FERC's Jurisdiction. First, Mississippi and several of its *amici* argue that FERC has no jurisdiction to establish wholesale rates for Grand Gulf 1 power or to allocate its costs to equalize the generation costs of MSU companies.[16] They note that Section 201(b) of the Federal Power Act provides that FERC "shall not have jurisdiction, except as specifically provided in this subchapter . . . over facilities used for the generation of electric energy" (J.S. App. 62a) and claim that this language somehow prohibits FERC from establishing just and reasonable rates for the sales of the output of Grand Gulf 1. On the merits, this claim is frivolous.[17] However, the short answer to this claim is that it cannot be raised in this case.

[16]Miss. Br., pp. 46–49; Ark. PSC Br., pp. 6-14; National Governors' Ass'n Br., pp. 12–20; National Ass'n of State Utility Consumer Advocates Br., pp. 18–23.

[17]This clause of Section 201(b) prohibits FERC from licensing generating facility or otherwise prescribing the location, size, type, or operations of such facilities. But FERC exercised no such jurisdiction over Grand Gulf 1. All the foregoing matters were determined by Mississippi authorities and the Nuclear Regulatory Commission.

(Footnote continued on following page)

The question whether § 201(b) could deprive FERC of jurisdiction over the Grand Gulf 1 rates was extensively litigated in the prior FERC proceedings. It was rejected by FERC in Opinions 234 and 234-A. J.S. App. 99a-103a, 155a-165a. It was unanimously rejected by a three-judge panel of the District of Columbia Circuit on direct review of the FERC decisions (*Mississippi Industries* v. *FERC*, *supra*, 808 F.2d at 1543–47), with *en banc* reconsideration denied. 822 F.2d 1103 (D. C. Cir. 1987). Petitions for certiorari were filed solely on this point, and petitioners urged that the fact the Court had decided to review the Mississippi Supreme Court's decision in this case required a grant of certiorari in *Mississippi Industries*. This Court denied certiorari less than two months ago, on December 14, 1987. 108 S. Ct. 500-01 (1987). These facts squarely foreclose the relitigation of this claim now. *City of Tacoma* v. *Taxpayers*, 357 U.S. 320 (1958).[18]

(Footnote continued from previous page)

All FERC did in Opinions 234 and 234-A, in contrast, is to establish rates and allocations for what are concededly wholesale sales of the *output* of a nuclear plant that other authorities licensed. This is what FERC does whenever it sets wholesale rates for any generating facility.

Moreover, even if FERC were deemed to be somehow exercising jurisdiction over generating facilities, Section 201(b) provides that FERC may exercise this jurisdiction when specifically authorized by other provisions of the Federal Power Act. Under Sections 205 and 206 of the Federal Power Act, FERC has explicit jurisdiction both to establish MSE's "just and reasonable" wholesale rates and to assure that the contracts that "affect rates" are just and reasonable. Thus, FERC Opinions 234 and 234-A are clearly within its statutory authority.

A more complete response to these contentions of Mississippi and its *amici* is contained in the November, 1987 Oppositions that FERC, SERI, and the other parties filed to the petitions for certiorari in *Arkansas Public Service Commission* v. *FERC*, and consolidated cases, Nos. 86-1380, 86-1424, & 87-469 (*cert. denied* Dec. 14, 1987).

[18]In *City of Tacoma* v. *Taxpayers*, this Court held that the exclusive means of litigating a challenge to FERC's jurisdiction is to raise it in proceedings before FERC and on direct review of FERC's order. Section 313 of the Federal Power Act and principles of *res judicata* prohibit the relitigation of the issue in a parallel state proceeding. 357 U.S. at 334-41.

Equitable Estoppel. Second, Mississippi argues that the doctrine of equitable estoppel supports the Mississippi Supreme Court's decision. However, Mississippi acknowledges (p. 43) that it is relitigating the challenges to FERC Opinions 234 and 234-A that were rejected by FERC and the District of Columbia Circuit in the prior federal proceedings. *See* Appellant's Br., pp. 15–16. Thus, this argument, too, is barred by Section 313 of the Federal Power Act, by *res judicata*, and by the Court's holding in *City of Tacoma*.

Beyond that, Mississippi's estoppel arguments rest on startling misstatements of the underlying facts and are baseless. Mississippi's principal claim derives from the terms of the 1974 Mississippi PSC certificate that authorized the construction of Grand Gulf 1. Mississippi does *not* claim that it could, or did, condition the issuance of this certificate on FERC's adoption of a particular allocation method. Thus, the novel contentions that Mississippi possesses this authority are not presented by this case.[19]

Rather, Mississippi relies (p. 39) on the fact that the certificate recites the fact that the MSU System then planned to "seek" FERC approval of a particular allocation method: that is, an amendment of the 1973 System Agreement in which MSE would become a party and the Grand Gulf 1 costs would be paid

[19]*See* National Governors' Ass'n Br., pp. 17–20; National Ass'n of State Utility Consumer Advocates Br., pp. 21–23. Quite plainly, FERC's jurisdiction over wholesale rates would be a nullity if the state that licenses construction of a plant can assert plenary authority over these rates and the underlying cost allocations.

The division of authority between state and federal authorities is thus clear. States may engage in the licensing of the facilities to the extent some other federal statute does not preempt this authority. *See Pacific Gas & Electric* v. *State Energy Resources Comm'n*, 461 U.S. 190 (1983). FERC, in turn, sets the rates for wholesale sales of the output of whatever plants state and federal authorities license, with FERC's "broad authority" recognized as an exception to state authority over the need for, and pricing of, electric generation. *Id.* at 205–06.

by "short" companies. *See* Miss. Supp. App., pp. 32–33.[20] Mississippi's Brief acknowledges (p. 39) that this had, indeed, been the Middle South System's intent at the time, that no misrepresentation was made, and that the only reason that the System proposed a different methodology is what the District of Columbia Circuit called the "unforeseen developments" of the late 1970s. *See* Appellant's Br., pp. 9–10. Mississippi's repeated statements (pp. 4–5, 19–21, 39–41) that the Middle South System conducted secret deliberations and hid the fact from the Mississippi authorities are false and unsupported by a single record citation.

However, the dispositive fact is that the failure of the Middle South System to propose this method did not affect any interests of the State of Mississippi. The Mississippi Attorney General and the Mississippi PSC intervened in the FERC proceedings and urged the adoption of the very allocation method that was referred to in the 1974 Mississippi PSC certificate. Mississippi's proposals were then rejected as "unjust, unreasonable, and discriminatory" and contrary to the Federal Power Act, on five separate occasions: twice by Administrative Law Judges, twice by FERC, and once by the District of Columbia Circuit. *See* Appellant's Br., pp. 11–16. Each held that the "unforeseen developments" of the late 1970s precluded any allocation of Grand Gulf 1 under the method contained in the 1973 System Agreement.

Against this background, it scarcely could be clearer that even if the Middle South System had proposed the 0% allocation for MP&L that Mississippi is advocating, it would have been rejected, just as FERC rejected the 0% allocation that was proposed for AP&L. Nothing MP&L and the Middle South System did, or did not do, affected any substantial right of Mississippi.

[20]Contrary to Mississippi's misstatement, this method would, based on the facts assumed in 1974, have produced a 38% allocation of Grand Gulf 1 to MP&L. R. 949-50, 1153, 1155. Due to the unforeseen intervening events, this method would produce a 0% allocation for MP&L today.

Mississippi's equitable estoppel argument is also based on statements that MP&L's President made in 1981 testimony in support of MP&L's application to acquire a 25% interest in the ISES coal generating facility in Arkansas. *See* Miss. Br., pp. 5, 40–41. These statements, made by a lay witness, suggest the legally erroneous view that the Mississippi PSC would not be bound by FERC's Grand Gulf 1 allocation. The complete answer to this claim is that FERC's authority and responsibility to set just and reasonable rates that bind the states cannot be foreclosed by statements made by a third party in a state regulatory proceeding.

Mississippi also states that the Mississippi PSC would not have authorized the ISES acquisition in 1981 if it had known that MP&L would thereafter be allocated a fixed 33% share of Grand Gulf 1's output. This is an astonishing statement. The 1981 Mississippi PSC order that authorizes MP&L's acquisition of a 25% share of this Arkansas coal-fired plant specifically found that MP&L is "require[d]" to "turn to coal and nuclear generation if the best interests of its customers are to be served in the future;" that "[t]he construction of the Grand Gulf Nuclear Station will help satisfy MP&L's need for nuclear generation in the foreseeable future;" and that the projected savings to MP&L's customers from the acquisition of the interest in the coal plant "was based on the assumption that [MP&L's] present share or allocation of the Grand Gulf Nuclear Plant of *approximately one-third would be fixed or remain at that level for the life of the Grand Gulf plant.*" Ex. 26, pp. 10, 13 (emphasis added).

The Mississippi PSC's actions in 1981 simply underscore that there was an extraordinary consensus during what Mississippi now terms the critical "period from 1977 until 1982." Miss. Br., p. 41. All then believed that MP&L's 33% interest in Grand Gulf 1's output would benefit its customers.

II. The Mississippi Supreme Court's Decision Is A "Final Judgment."

The sole issue that the Mississippi Supreme Court decided and the only issue before the Court is whether federal law preempts the Mississippi PSC from investigating the prudence of MP&L's

Grand Gulf 1 expenses. Mississippi and one *amicus* (New Orleans) nevertheless contend that the Mississippi Supreme Court's decision is not a "final judgment" and cannot be reviewed at this time. This argument is extraordinary. As the Court necessarily recognized in issuing its two prior stay orders, MP&L will suffer "trapped costs" of over $600 million and immediate bankruptcy if the Mississippi Supreme Court's mandate issues—all because the Mississippi PSC would be pursuing an investigation it has no jurisdiction to make. At least two of the recognized exceptions to ordinary finality requirements are thus satisfied. *See Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 477-87 (1975). It is only by misstating the Mississippi Supreme Court's holding that Mississippi can argue otherwise.[21]

First, New Orleans' arguments demonstrate that the Mississippi Supreme Court "finally decided" a federal question that "will survive and require decision regardless of the outcome of future state-court proceedings." 420 U.S. at 480. New Orleans recognizes (pp. 11-12) that the Mississippi Supreme Court held that MP&L cannot recover any of its Grand Gulf 1 expenses "*before*" the Mississippi PSC makes its own determination of their "prudency" and that this holding, by its terms, requires a refund of hundreds of millions in MP&L's Grand Gulf 1 prior collections and a roll-back of MP&L's existing rates. Indeed, six days before this Court's June 1, 1987 stay order, the Mississippi PSC ordered precisely that. J.S. App. 200a. In short, New Orleans recognizes that the Mississippi Supreme Court finally resolved a major portion of this case in a manner that threatens irreparable harm to MP&L.[22]

[21]For example, Mississippi asserts (p. 28) that "[n]owhere in the decision of the Mississippi court is it ordered that the MPSC is not to give binding effect to the FERC order allocating Grand Gulf costs." However, that is precisely what the Mississippi Supreme Court did. The Mississippi Supreme Court held that FERC's finding that a 33% allocation of Grand Gulf 1 to MP&L will result in just and reasonable rates does not bind the Mississippi PSC. J.S. App. 13a-20a.

[22]This fact forecloses the arguments (*e.g.*, Miss. Br., p. 44) that MP&L's Commerce Clause claim is not ripe. Mississippi's conduct im-
(Footnote continued on following page)

However, New Orleans argues that there is no need to decide the case now because this Court stayed the Mississippi Supreme Court's mandate on June 1, 1987, and New Orleans urges that this stay can be continued in effect pending the completion of the future state proceedings. This argument is simply an admission of the facts that establish the Court's jurisdiction over this appeal now.

The Mississippi Attorney General, in contrast, argues (pp. 23–24) that the Mississippi PSC will, on remand, have statutory authority to prevent MP&L's imminent bankruptcy by authorizing MP&L to continue to collect its Grand Gulf 1 expenses and to retain all amounts previously collected. This argument is startling. The Mississippi Attorney General himself previously filed the motion that urged that an immediate rollback and refund are now required by Mississippi law. *See* Mississippi Attorney General's Petition To Roll Back The Authorized Rates Of MP&L, pp. 3–4 (filed May 26, 1987). And this motion has already been granted in the face of the Mississippi PSC's prior findings (J.S. App. 29a) that MP&L's bankruptcy would result.

Finally, and in any event, the Mississippi Supreme Court's decision would be a final judgment even if its sole consequence were to require the Mississippi PSC to investigate the "prudency" of MP&L's Grand Gulf 1 expenditures. FERC and MP&L are challenging Mississippi's jurisdiction to make this determination. A long line of decisions of this Court, and "sound judicial administration," establish that such challenges are reviewable once the highest court in a state has upheld the state's jurisdiction. *See* Appellant's Br., pp. 30–31 & n.28; *see also Shaffer* v. *Heitner*, 433 U.S. 186, 195-96 n.12 (1977).

(Footnote continued from previous page)
poses a far greater, and far more immediate, burden than did the state's conduct in *New England Power Co.* v. *New Hampshire*, 455 U.S. 331, 343–44 n.10 (1982). And the consequences are not limited to Mississippi. Even in the absence of a decision by this Court, New Orleans on February 4, 1988, disallowed $135 million of the Grand Gulf 1 expenses of MP&L's affiliate (NOPSI) on "prudence" grounds.

CONCLUSION

For the reasons stated, the judgment of the Mississippi Supreme Court should be reversed.

Respectfully submitted,

REX E. LEE*
GEORGE L. SAUNDERS, JR.
DAVID W. CARPENTER
1722 Eye Street, N.W.
Washington, D.C. 20006
(202) 429-4000

ROBERT R. NORDHAUS
HOWARD E. SHAPIRO
1050 Thomas Jefferson St., N.W.
Washington, D.C. 20007
(202) 298-1800

JAMES K. CHILD, JR.
HENDERSON S. HALL, JR.
600 Heritage Building
Post Office Box 651
Jackson, Mississippi 39205
(601) 354-2385

Of Counsel:

WISE CARTER
CHILD & CARAWAY
SIDLEY & AUSTIN
VAN NESS, FELDMAN,
SUTCLIFFE & CURTIS

Attorneys for Appellant

Dated: February 9, 1988

**Counsel of Record*

AMICUS CURIAE

BRIEF

(11)

No. 86-1970

In the Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY, APPELLANT

v.

STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, AND MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

CHARLES FRIED
Solicitor General

LOUIS R. COHEN
Deputy Solicitor General

RICHARD J. LAZARUS
Assistant to the Solicitor General
Department of Justice
Washington, D.C. 20530
(202) 633-2217

CATHERINE C. COOK
General Counsel

JEROME M. FEIT
Solicitor

JOHN N. ESTES III
Attorney
Federal Energy Regulatory Commission
Washington, D.C. 20426

34 pp

QUESTION PRESENTED

Whether *Nantahala Power & Light Co.* v. *Thornburg*, No. 86-568 (June 17, 1986), requires a state public utility commission to allow an electric utility to recover, in retail rates, its share, as determined by the Federal Energy Regulatory Commission, of the costs of an electric power generating facility that supplies power to the utility and sister utilities in three other states.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

In the Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY, APPELLANT

v.

STATE OF MISSISSIPPI EX REL. EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, AND MISSISSIPPI LEGAL SERVICES COALITION

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

BRIEF FOR THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION AS AMICI CURIAE

INTEREST OF THE UNITED STATES AND THE FEDERAL ENERGY REGULATORY COMMISSION

Part II of the Federal Power Act, 16 U.S.C. (& Supp. IV) 824 *et seq.*, gives the Federal Energy Regulatory Commission (FERC) exclusive regulatory authority over the wholesale sale and the transmission of electric energy in interstate commerce. FERC is responsible for ensuring that all rates or charges made, demanded, or received by a public utility for or in connection with the transmission or sale of electric energy in interstate commerce are "just and reasonable" (16 U.S.C. 824d(a)). This case was preceded by FERC's decision, upon examination of the justness and reasonableness of two agreements filed with FERC by the members of a four-state public utility holding company system, that the four operating companies of the system shall purchase the capacity of a particular

nuclear power plant owned by the system in proportions deemed just and reasonable by FERC. The Mississippi Supreme Court held in this case that the Mississippi Public Service Commission may not allow the system operating company serving customers in Mississippi to recover this FERC-determined cost unless the state commission first determines that this cost was prudently incurred by the Mississippi operating company. If allowed to stand, the Mississippi Supreme Court's decision would effectively nullify FERC's allocation of capacity and costs among the four operating companies. FERC participated as amicus curiae in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986), because the decision of the state supreme court in that case similarly threatened to nullify an exercise of FERC's exclusive statutory authority.

STATEMENT

In a FERC administrative proceeding in which the Mississippi Public Service Commission (MPSC) and the Mississippi Attorney General participated, FERC allocated the capacity and costs of a jointly planned nuclear power plant, Grand Gulf Unit No. 1 (Grand Gulf 1), among the four electric utility subsidiaries of Middle South Utilities, Inc. (MSU): Mississippi Power & Light Company (MP&L), which operates in Mississippi, and three other utilities, which operate in three other states. FERC concluded that its allocation would result in a just and reasonable sharing of the costs among the four companies. In a review proceeding in which MPSC and the Mississippi Attorney General again participated, the Court of Appeals for the District of Columbia Circuit affirmed FERC's determination that it had jurisdiction to determine the proportions in which the four companies shall bear these costs. In the present case, the Mississippi Supreme Court ruled that MPSC may not permit MP&L to increase its charges to retail customers in Mississippi, to reflect the Grand Gulf 1 costs allocated to MP&L by FERC, "without first determining that the expenses were prudently incurred" (J.S. App. 2a).

A. The Middle South System And Grand Gulf Unit No. 1

Appellant MP&L is one of four operating electric utility companies that are wholly-owned subsidiaries of Middle South Utilities (MSU), a public utility holding company established in 1949 under Title I of the Public Utility Holding Company Act of 1935 (PUHCA), 15 U.S.C. 79 *et seq.*[1] See *Electric Power & Light Co.*, 29 S.E.C. 52 (1949). The other subsidiary operating companies are Louisiana Power & Light Co. (LP&L), Arkansas Power & Light Co. (AP&L), and New Orleans Public Service, Inc. (NOPSI). These four companies operate as a highly integrated power pool. They sell and exchange electricity at wholesale across state lines, to each other as well as to outside companies, and they also sell electricity at retail in separate service areas in four states. Transactions among the operating companies in the Middle South system, including the sale and exchange of capacity and energy, have been governed by a series of "System Agreements" filed with FERC. These agreements have provided the contractual basis for planning and operating the companies' generating units on a single-system basis; they have also provided mechanisms for equalizing cost imbalances among the four companies that result from the system's method of planning and operating the units. All energy on the Middle South system is centrally dispatched from the system's dispatch center at Pine Bluff, Arkansas. J.S. App. 3a-4a; *Middle South Services, Inc.*, 30 F.E.R.C. ¶ 63,030, at 65,141-65,142 (1985); *Middle South Energy, Inc.*, 26 F.E.R.C. ¶ 63,044, at 65,095 (1984).

A systemwide Operating Committee has historically coordinated the planning of new generating capacity for the system and has attempted to equalize the costs of additional capacity among the four operating companies (30 F.E.R.C. at 65,142; 26 F.E.R.C. at 65,100). In the late

---

[1] MSU owns all the common (the only voting) stock of the operating companies. The operating companies have outstanding preferred stock and bonds held by other persons. See J.S. App. 4a.

1960s, the MSU system sought to meet projected increases in demand and to diversify its fuel base (principally oil and gas) by adding coal and nuclear generating units (J.S. App. 115a-121a). The Middle South system initiated several nuclear power projects, including Grand Gulf, for these purposes. In an effort to equalize costs and promote economies of scale, the Operating Committee has, in effect, rotated the responsibility for financing, building, and operating these new generating units among the four operating companies (*id.* at 115a-120a; 26 F.E.R.C. at 65,099-65,101).

Under the original plan, MP&L was assigned responsibility for financing and constructing Grand Gulf 1, both "to meet system load and, in particular, the load of MP&L" (26 F.E.R.C. at 65,101); NOPSI was assigned responsibility for financing and constructing Grand Gulf Unit No. 2 (Grand Gulf 2). Responsibility for construction of both units soon shifted to MP&L, however, because of siting problems with NOPSI's jurisdiction. When it subsequently became apparent that MP&L could not finance the construction of even one of the units, MSU made a system decision in 1974 to form a generation subsidiary, Middle South Energy (MSE) (now Systems Energy Resources, Inc.), to finance the project. MSE acquired from MP&L all of its right, title, and interest in the Grand Gulf project. J.S. App. 118a.

By the late 1970s, it became evident that Grand Gulf's capacity would not be needed immediately to meet demand, which was lower than predicted in earlier forecasts (26 F.E.R.C. at 65,102-65,103). MSU continued to build the Grand Gulf units on the assumption that the overall (fixed plus variable) cost of Grand Gulf power per kilowatt hour would, partly because of the relatively low cost of nuclear fuel, be lower than that of alternative energy sources, and that MSE would sell the capacity and energy of the Grand Gulf plants at wholesale to the four operating companies, in proportions to be determined later (*ibid.*). The investment cost of those plants, however, continued to increase dramatically because of regulatory delay, additional construction requirements, inflation, and increased financing costs. As a result, the system suspended construction of Grand Gulf 2,[2] and, although the investment cost of both Grand Gulf units had been projected at $1.2 billion, the investment cost of Grand Gulf 1 alone proved to be approximately $3 billion. Although fuel costs are lower for Grand Gulf 1 than for other system sources, the overall cost per kilowatt hour is higher for Grand Gulf than for any other system source of power (except for one other expensive nuclear plant contemporaneously built by LP&L). 30 F.E.R.C. at 65,144-65,145; 26 F.E.R.C. at 65,101-65,103; see J.S. App. 122a.

B. The Federal Proceedings

1. Under Part II of the Federal Power Act, 16 U.S.C. (& Supp. IV) 824 *et seq.*, FERC has exclusive regulatory authority over the transmission of electric energy in interstate commerce and the wholesale sale of electric energy in interstate commerce. FERC is responsible for ensuring that all rates or charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy in interstate commerce, as well as all rules, regulations, practices, and contracts affecting those rates or charges, are just and reasonable (16 U.S.C. 824(a)).

In 1982, the MSU companies filed with FERC a 1982 System Agreement, which set forth the terms and conditions for coordinated operations and wholesale transactions among the four operating companies (except the sale of power from Grand Gulf 1), including a scheme of "capacity equalization payments" which are designed to ensure that each company contributes proportionately to the total costs of generating power on the system.[3] The

---

[2] Grand Gulf 2 has not commenced operation, and allocation of its costs is not at issue in this case.

[3] These payments are intended to compensate for the imbalances created by the system's rotational scheme of adding capacity: the last company to add capacity would, because the plant is sized for

companies also filed with FERC a Unit Power Sales Agreement (UPSA), which established wholesale rates for MSE's sale of Grand Gulf 1 capacity and energy; the UPSA obliged the four operating companies to purchase the following specified percentages of Grand Gulf capacity: LP&L, 38.57%, MP&L, 31.63%, NOPSI, 29.80%, and AP&L, 0% (J.S. App. 81a).[4]

FERC assigned the two contracts to two different administrative law judges to consider whether the contracts were "just and reasonable," as required by the Federal Power Act. MPSC, the Mississippi Attorney General, and Mississippi Legal Services Coalition participated in both administrative proceedings. After administrative hearings, the judges concluded in two separate decisions, rendered in February 1984 and February 1985, that the agreements, as filed, were not just and reasonable, and were unduly discriminatory, because they allowed AP&L to avoid any financial responsibility for the costs associated with Grand Gulf 1. *Middle South Services, Inc.*, 30 F.E.R.C. ¶ 63,030, at 65,170-65,173 (1985) (1982 System Agreement); *Middle South Energy, Inc.*, 26 F.E.R.C. ¶ 63,044, at 65,105-65,108 (1984) (UPSA).

a. FERC reviewed the decisions of the two administrative law judges, and issued its decision in June 1985. *Middle South Energy, Inc.*, 31 F.E.R.C. ¶ 61,305 (J.S. App. 74a-152a), on reh'g, 32 F.E.R.C. ¶ 61,425 (J.S. App. 154a-195a), aff'd, *Mississippi Industries* v. *FERC*, 808 F.2d 1525, reh'g granted and vacated in part, 822 F.2d 1104, 1105 (D.C. Cir. 1987), petitions for cert. pending, Nos. 86-1380, 86-1424 & 87-469. FERC concluded that the UPSA and the 1982 System Agreement, as filed by the Middle South companies, would result in unjust, unreasonable, and unduly discriminatory allocations of generating costs among the operating companies and "that some form of equalization of nuclear plant costs is necessary to achieve just, reasonable, and nondiscriminatory rates among the MSU operating companies" (J.S. App. 122a (footnote omitted)). FERC determined, moreover, that the "most equitable allocation" would be for the operating companies to share in the system's total investment in nuclear capacity (four units, including Grand Gulf 1) "roughly in proportion to each company's share of System demand" (*id.* at 123a (footnote omitted)). On that basis, FERC ordered the following allocation of Grand Gulf 1 capacity and costs: MP&L, 33%, AP&L, 36%, LP&L, 14%; and NOPSI, 17% (*ibid.*).

FERC made two pertinent factual findings. First, FERC found that "the Middle South companies constitute a highly coordinated integrated electric system," which historically has "roughly equalized" generating costs among the four operating companies (J.S. App. 104a, 121a). FERC stressed that "this coordination and integration results in planning, construction, and operations which are conducted primarily for the system as a whole" (*id.* at 104a). FERC specifically found (*id.* at 115a-120a) that Grand Gulf 1 had been planned "to meet MP&L's needs, to meet System needs, and to meet the System goal of diversifying fuel mix." Second, FERC found that Grand Gulf 1 was part of a reasonable system plan to diversify the fuel base by developing nuclear power to meet anticipated growth in demand (*id.* at 115a-126a). FERC affirmed (*id.* at 146a) the conclusion of one of the administrative law judges that the MSU system's decisions both to begin and to complete construction of Grand Gulf 1 were prudent (26 F.E.R.C. at 65,112-65,113).

FERC rejected contentions advanced by several parties, including the Mississippi parties, against the proposed

system needs, typically have contributed more than its share of costs. J.S. App. 84a-85a; 30 F.E.R.C. at 65,168.

[4] The allocation distributed among the four operating companies the "capacity" of the plant (that is, the capacity to produce a certain amount of energy), the entitlements to whatever energy is produced from that capacity, and the costs of both the capacity (the upfront "investment" costs of constructing the plant and other fixed costs) and the energy (including fuel and other variable costs).

allocation and in favor of other allocations more favorable to their interests. FERC rejected a proposal of the Mississippi parties that the capacity and costs of Grand Gulf 1 be allocated instead under the terms of the 1973 System Agreement. FERC determined that allocation on that basis would be "inequitable and discriminatory because it would result in MP&L avoiding all responsibility for Grand Gulf for approximately 10 years, after which time it would enjoy the benefits of the project in the less expensive years" (J.S. App. 124a-125a n.19).[5]

b. FERC subsequently clarified its June 1985 decision in the course of denying several petitions for rehearing (J.S. App. 154a-192a). FERC took that occasion to reject submissions that it lacked authority to reallocate the obligation to purchase Grand Gulf capacity and that FERC's allocation failed to consider the needs of individual operating companies (*id.* at 172a-192a). According to FERC (*id.* at 184a), when, as in the Middle South system, the operating companies "approach power planning on a system-wide basis, whereby the individual companies' needs are the component parts of the System power plan[,] [i]mplementation of the system plan * * * requires that the individual companies' needs be subsumed by the greater interests of the entire System." For this reason, FERC concluded, no one operating company could now avoid financial responsibility for Grand Gulf, which they jointly decided to build, finance, and allocate, as if the one company were an independent entity

[5] FERC rejected arguments by MPSC and the Mississippi Attorney General that the proposed allocation violated the doctrine of equitable estoppel because it was contrary to representations made by MP&L and MSE to MPSC, which MPSC allegedly relied upon in granting a certificate of public convenience and necessity to construct Grand Gulf 1 (J.S. App. 90a). According to FERC, "a State [C]ommission could not reasonably rely on representations in State proceedings * * * since [FERC] alone has jurisdiction over the [allocation issue]" and, in any event, "the doctrine cannot operate to bind [FERC] since [it] made no representations in and w[as] not a party to any of the State certification proceedings" (*id.* at 103a). The D.C. Circuit agreed (808 F.2d at 1549-1550).

free to consider only its own immediate needs (*id.* at 157a; see 26 F.E.R.C. at 65,113).

2. On petition for review of FERC's orders, MPSC and the appellees here, the Mississippi Attorney General and the Mississippi Legal Services Coalition, as well as parties from the other three states, challenged FERC's allocation. The Court of Appeals for the District of Columbia Circuit unanimously affirmed as to FERC's jurisdiction but, on rehearing, ultimately vacated the allocation itself, remanding to FERC for fuller explanation. *Mississippi Industries* v. *FERC*, 808 F.2d 1525, reh'g granted and vacated in part, 822 F.2d 1104 (D.C. Cir. 1987), petitions for cert. pending, Nos. 86-1380, 86-1424 & 87-469.

a. Relying on this Court's decisions in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986), and *Pennsylvania Water & Power Co.* v. *FPC*, 343 U.S. 414, 422-423 (1952), the court of appeals upheld FERC's authority under the Federal Power Act to allocate the capacity and costs of Grand Gulf 1 (808 F.2d at 1539-1543). The court emphasized that "[a] consistent line of judicial precedent supports FERC's authority to approve and/or modify the terms of the pooling and coordination agreements of closely integrated power systems" (*id.* at 1545) and that Grand Gulf 1 was "built and planned on a profoundly integrated basis" (*id.* at 1540).

The court of appeals, like FERC, specifically rejected the various objections raised by the Mississippi parties—MPSC, the Mississippi Attorney General, and Mississippi Legal Services Coalition—to FERC's allocation. The court concluded (808 F.2d at 1563-1565), with "little difficulty," that FERC had properly rejected the Mississippi parties' proposed allocation of the capacity and costs of Grand Gulf. The court also rejected (*id.* at 1548) suggestions that the potential impact of FERC's allocation on retail rates required its invalidation.

b. The court of appeals initially affirmed, over Judge Bork's partial dissent, FERC's specific allocation of

Grand Gulf capacity and costs (808 F.2d at 1553-1566); subsequently, however, the court granted rehearing and vacated the portion of its judgment concerning the specific allocation, and the related portions of its opinion (822 F.2d 1104 (1987); 808 F.2d at 1568-1569 (Bork, J., dissenting)). In accordance with Judge Bork's dissent, the court remanded the case to FERC "for reconsideration of the decision to equalize the capacity costs of all nuclear plants, and for an explanation of the criteria used to determine what constitutes 'undue discrimination' and of why [FERC's] ultimate decision is not unduly discriminatory" (822 F.2d at 1105).[6] On November 30, 1987, FERC issued an order on remand that reaffirmed and further explained its allocation decision. *System Energy Resources, Inc.*, 41 F.E.R.C. ¶ 61,238 (1987).

C. Mississippi State Proceedings

1. Since Grand Gulf 1 went into service on July 1, 1985, MSE has billed the four operating companies, including MP&L, on a monthly basis in accordance with FERC's allocation. MP&L accordingly sought approval from MPSC to recover its Grand Gulf payments (about $27 million per month) in retail rates. MPSC granted full retail recovery of those costs but "phased in" the increase over a ten-year period, so that consumers would pay less than the full amount during an initial period and gradually pay the difference (plus financing charges) over a later period. J.S. App. 30a-31a.

2. The Mississippi Supreme Court reversed (J.S. App. 2a-22a). The court ruled that, under Mississippi law

[6] On April 3, 1987, the panel had previously denied rehearing and the court of appeals had granted rehearing en banc to consider the terms of FERC's allocation (814 F.2d at 773). On June 24, 1987, the court of appeals issued two separate orders. In the first, the court, sitting en banc, vacated its prior order setting the case for rehearing en banc, and reinstated the portions of the opinion and judgment it had earlier vacated (822 F.2d at 1103-1104). In the second, the panel vacated its earlier order denying the petitions for rehearing, granted the petitions, and reversed a portion of its opinion and judgment of January 6, 1987, concerning FERC's allocation (*id.* at 1104-1105).

(Miss. Code Ann. § 77-2-39 (1972)), MPSC "must review the prudency of an investment such as Grand Gulf before it can enact rates based on its cost" to "determine whether MP&L, MSE[,] and MSU acted reasonably when they constructed Grand Gulf 1, in light of the change in demand for electric power in this state and the sudden escalation of costs" (J.S. App. 19a-20a).

The state supreme court rejected (J.S. App. 14a-16a) MP&L's claim that MPSC is required, under *Nantahala*, to allow MP&L to pass through its FERC-allocated share of Grand Gulf costs in retail rates without undertaking any independent "prudency" review. According to the state court (J.S. App. 15a), MPSC would plainly have jurisdiction to consider "prudency" if MPSC had itself built Grand Gulf, and the court did not believe that the Supremacy Clause required a different result just "because Grand Gulf is owned by an out-of-state corporation." The court argued (*ibid.* (quoting *Nantahala*, slip op. 19) (emphasis omitted)) that *Nantahala* is not to the contrary because there this Court had assumed "that a particular quantity of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere," but concluded that no lower-cost alternative was available in the circumstances of that particular case. This case, according to the state court (J.S. App. 15a), is unlike *Nantahala* because here "there is no doubt that Mississippians do *not* need the power provided by Grand Gulf, and that lower cost power is available elsewhere (in fact, by plants owned by MP&L)."

Finally, the state court concluded (J.S. App. 17a-18a) that preemption is inappropriate because FERC was never presented with, and never addressed, the question whether it was prudent to complete Grand Gulf 1 and continue its operation. The court stated (*id.* at 17a) that FERC had simply assumed that it was appropriate to complete construction of Grand Gulf 1, the D.C. Circuit had never addressed the issue in reviewing FERC's decision, and, as a result, the state court had "yet to see

MP&L, MSE[,] or MSU justify putting Grand Gulf on line at its exorbitant cost to ratepayers." [7]

Justice Robertson dissented (J.S. App. 23a). Relying on this Court's decision in *Nantahala*, he concluded that "our decision this day is in an area wholly preempted by authority granted by the Congress to [FERC]" (*ibid.*).

3. On remand, MPSC accordingly rescinded (J.S. App. 199a-200a) its September 16, 1985, rate increase and ordered MP&L to submit a plan for refunding all of its prior recovery of Grand Gulf 1 expenses from the retail ratepayers. On June 1, 1987, this Court granted a stay of the Mississippi Supreme Court's judgment conditioned upon MP&L posting a good and sufficient bond, in manner and amount to be determined by the Mississippi Supreme Court. On June 23, 1987, this Court granted a stay of the Mississippi Supreme Court's subsequent order that MP&L could not recover its Grand Gulf expenses until it had posted the required bond.

SUMMARY OF ARGUMENT

The decision of the Mississippi Supreme Court is flatly inconsistent with this Court's decision in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986). In *Nantahala*, this Court affirmed the rule that "a state utility commission setting retail [rates] must allow, as reasonable operating expenses, costs incurred as

[7] The state court also ruled (J.S. App. 21a-22a) that MPSC must join MSU, the parent holding company, and MSE, the company that owns Grand Gulf 1, as parties in its review of the prudence of the Sales Agreement. In support, the court suggested an additional basis for its broader ruling that MPSC's authority has not been preempted by federal law. The court concluded that where, as in this case, agreements between the operating companies, including MP&L, were "suspect" because of the absence of arms-length bargaining, *Nantahala* requires only preemption of a state public utility commission's evaluation of a "FERC approved rate[]" (J.S. App. 21a (quoting *Nantahala*, slip op. 12)); *Nantahala* did not, the court said, eliminate the state commission's jurisdiction to examine the "prudency" of the "suspect" agreements (J.S. App. 21a).

a result of paying a FERC-determined wholesale price" (slip op. 11). "[A] State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable" (*id.* at 13).

The amounts now being charged by MSE to MP&L for Grand Gulf power *are* "FERC-approved wholesale rates." In proceedings in which MPSC and the Mississippi Attorney General participated, FERC determined that justness and reasonableness required MP&L, which draws all of its energy from sources within the MSU system, to purchase 33% of the capacity of Grand Gulf 1. FERC's authority to impose this obligation on MP&L was squarely affirmed by the D.C. Circuit. The decision of the state court, which bars MP&L from passing the cost of its FERC-allocated share of Grand Gulf 1 capacity and energy on to its retail customers and therefore forces that cost to be borne by its parent MSU or its sister utilities in other states, effectively nullifies a FERC decision in which the State of Mississippi fully participated.

Appellees attempt to justify the state court's decision on the grounds, first, that FERC has not authoritatively determined whether it was "prudent" to build Grand Gulf 1 and the state may therefore do so, and, second, that *Nantahala* leaves a state utility commission free to determine that the *quantity* of power procured from a particular source is excessive and imprudent, because the utility's needs can be met from less expensive sources, even though the *price* of the higher cost power has been approved by FERC and must therefore be accepted as reasonable. But neither of these "prudence" inquiries is open to the state here. First, the question whether the costs of Grand Gulf 1 were prudently incurred, so that MSE may properly reflect 100% of those costs in the amounts it charges the operating companies in interstate wholesale transactions with them, is plainly within the exclusive jurisdiction of FERC; any contention that the wholesaler (MSE) and its shareholders should absorb some of these costs rather than pass them through to the operating companies must be made to FERC. Sec-

ond, MP&L has no alternative to buying system power; this is a case like *Nantahala* itself, where all of the relevant sources of electric power are within the utility system and the sole question—one that only FERC can fairly resolve—is how the benefits and burdens of those sources should be shared between affiliated companies doing business in different states.

Appellees also argue that this Court lacks jurisdiction to hear this case because the state supreme court remanded for further proceedings before MPSC. Review is appropriate, however, because the Mississippi Supreme Court has *finally* denied MP&L's right to recover substantial Grand Gulf 1 expenses, incurred pursuant to FERC's allocation determination, that MP&L will have absorbed prior to completion of the MPSC proceedings on remand. See *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 480-481 (1975). Review is also appropriate because the preemption claim challenges the very legitimacy of the further MPSC proceedings; hence, refusal to hear the preemption claim now would "seriously erode federal policy" (*id.* at 482-483).

ARGUMENT

THE STATE OF MISSISSIPPI MAY NOT DENY MISSISSIPPI POWER & LIGHT RECOVERY OF ITS FERC-ALLOCATED SHARE OF THE COSTS OF GRAND GULF 1 PENDING A STATE DETERMINATION OF WHETHER THOSE COSTS WERE PRUDENTLY INCURRED

MSE, which built and operates Grand Gulf 1, sells its capacity and energy at wholesale in interstate commerce to the four operating companies with which it is affiliated. The four operating companies also derive all of their other energy from shared sources within the MSU system. The inherently interstate arrangements for the sale of Grand Gulf 1 capacity and energy and the sharing of other system capacity and energy are set forth in agreements filed with FERC and reviewed by FERC in proceedings in which all parties to the present case participated. The questions (a) whether MSE as wholesaler may charge the operating companies for Grand Gulf power at rates that reflect 100% of the costs of the facility or must (together with its parent MSU and the public shareholders) absorb some portion of those costs on the ground that they were not prudently incurred, and (b) how the Grand Gulf costs that are charged to the operating companies should be shared among four companies operating a "highly coordinated integrated electric system," are both within the exclusive jurisdiction of FERC.

The state court barred MP&L from recovering costs it is currently incurring pursuant to a FERC determination, until MPSC conducts a "prudency" inquiry into one or both of the foregoing questions. That decision flatly violates this Court's ruling in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986). In *Nantahala*, the Court affirmed the well established rule that "a state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred as a result of paying a FERC-determined wholesale price" (slip op. 11). "[A] State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable" (*id.* at 13). If allowed to stand, the state court ruling would, contrary to *Nantahala*, effectively nullify FERC's decision here, by barring MP&L from passing the costs of its FERC-allocated share of Grand Gulf 1 capacity on to its customers, unless and until MPSC reaches a favorable resolution of questions it has no power to decide.

A. The Decision Of The Mississippi Supreme Court Is A "Final Judgment" Within The Meaning Of 28 U.S.C. 1257

Appellees (Miss. Mot. to Dismiss 11-14)[8] argue that this Court lacks jurisdiction because the Mississippi Su-

[8] "Miss. Mot. to Dismiss" refers to the motion to dismiss filed by appellees State of Mississippi, et al. "MLSC Mot. to Dismiss" refers to the motion to dismiss filed by appellee Mississippi Legal Services Coalition.

preme Court remanded the case to MPSC for further proceedings and, hence, its judgment is not "final," within the meaning of 28 U.S.C. 1257. The remand for further state administrative proceedings does not, however, deprive this Court of jurisdiction.

This Court "has recurringly encountered situations in which the highest court of a State has finally determined the federal issue present in a particular case, but in which there are further proceedings in the lower state courts to come." *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 477 (1975). See generally R. Stern, E. Gressman, S. Shapiro, *Supreme Court Practice* 129 (1986). The Court has "treated the [final] decision on the federal issue as a final judgment for the purposes of 28 U.S.C. § 1257 * * * [,] without awaiting the completion of the additional proceedings," in "at least four categories of such cases" (*Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. at 477). The Mississippi Supreme Court's decision falls within at least two of these categories.

The "federal issue" is whether MPSC *may* deny MP&L recovery of its FERC-allocated share of Grand Gulf 1 costs, unless and until MPSC finds that those costs were prudently incurred. That "federal issue, finally decided by the highest court in the State, will survive and require decision regardless of the outcome of future state-court proceedings" (*Cox Broadcasting Corp.* v. *Cohn*, 470 U.S. at 480). Even if MPSC rules in favor of MP&L on the "prudency" issue and the ruling is sustained on appeal, the federal issue will survive because the state court ruling permits "trapping" of MP&L's costs incurred while the prudency issue is being decided and there is no indication that that ruling could or would be revisited. Specifically, the decision of the Mississippi Supreme Court mandated the immediate refund by MP&L of the $200 million in Grand Gulf 1 costs already collected by MP&L and a rescission of retail rates that allowed for MP&L's recovery of its share of those continuing costs. The proceedings on remand, however, will concern only MP&L's right to recover its FERC-allocated share of

Grand Gulf 1 costs prospectively. MP&L's right to recover the Grand Gulf 1 costs it incurs in the meantime has been finally denied by the state supreme court.[9]

The Mississippi Supreme Court's decision constitutes a "final judgment" for purposes of this Court's appellate jurisdiction for a second reason as well. "[I]f a refusal immediately to review the state court's decision will seriously erode federal policy, this Court has entered and decided the federal issue, which itself has been finally determined by the state courts," when "the party seeking review here might prevail on the merits on nonfederal grounds, thus rendering unnecessary review of the federal issue by the Court, and [when] reversal of the state court on [the] federal issue would be preclusive of any further litigation" (*Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. at 482-483). This case falls within the spirit of that rule.

Here, reversal of the Mississippi court's ruling would completely eliminate the need for further proceedings before MPSC concerning whether the costs of Grand Gulf 1 were prudently incurred. And refusal to hear the case now would frustrate important federal policy: the federal preemption claim challenges the legitimacy of the very MPSC proceedings upon which appellees rely in claiming that the state court's decision was not "final." Conversely, although (as noted above) MP&L would apparently suffer trapped interim costs even if it is wholly

[9] Moreover, MP&L is required to pay its FERC-allocated share of Grand Gulf 1's cost (approximately $27 million each month) on a continuing basis. If this Court were ultimately (but only after further state proceedings) to rule that MP&L's right to pass through Grand Gulf 1 costs should not have been delayed for a state "prudency" inquiry, it may not then be practical (even if lawful) to recover fully the present value of the interim costs through "catch-up" rates. That is presumably why this Court stayed the MPSC's refund and rescission order. "[I]mmediate rather than delayed review would be the best way to avoid 'the mischief of economic waste and of delayed justice.'" *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. at 477-478 (quoting *Radio Station WOW, Inc.* v. *Johnson*, 326 U.S. 120, 124 (1945)).

successful in the contemplated MPSC proceedings, such costs may, as noted (see note 9, *supra*), have become largely irrecoverable, leaving no substantial live issue for this Court. Where, as in this case, the power of the state tribunal to proceed is at the heart of the preemption claim finally decided by the state court and federal policy would be seriously undermined by the remand itself, it is proper to deem that "issue separable from the merits and ripe for review in this Court." Cf. *Construction Laborers* v. *Curry*, 371 U.S. 542, 550 (1963).

B. FERC Has Exclusive Jurisdiction To Determine Whether Grand Gulf 1 Was A Prudent Undertaking For The MSU System As A Whole And To Determine The Allocation Of Grand Gulf Costs Among The Component Companies Of The MSU System

The Mississippi Supreme Court and appellees assert (J.S. App. 17a-18a; Miss. Mot. to Dismiss 17-18; MLSC Mot. to Dismiss 10) that MPSC can, in establishing MP&L's retail rates, consider whether the costs of Grand Gulf 1 were prudently incurred, because FERC did not actually make such an inquiry in reviewing the agreements governing the wholesale sale of Grand Gulf power by MSE to the operating companies. Appellees also argue (Miss. Mot. to Dismiss 17, 19-25; see also Miss. Mot. to Dismiss App. 56, 60, 62, 66) that MPSC may deny MP&L the right to recover in retail rates its share of the costs of Grand Gulf 1 on the basis of some prudence determination that would not interfere with FERC's jurisdiction or its rulings in this matter. Both arguments are wrong.

1. Sales of Grand Gulf 1 capacity and energy by MSE to the four operating companies are interstate wholesale transactions over which FERC has exclusive jurisdiction. A wholesale rate is unjust and unreasonable, and may be unduly discriminatory, if it allows a public utility to recover costs that were not prudently incurred, and such a rate may be challenged before FERC. See *New England Power Co.*, 31 F.E.R.C. ¶ 61,047, at 61,081-61,084 (1985),

aff'd, 800 F.2d 280 (1st Cir. 1986). But the contention that Grand Gulf costs were not prudently incurred and may not be reflected in MSE's charges is one that may be made only to FERC. Regardless of the exact extent to which that issue was actually raised and decided in the FERC proceedings,[10] MPSC has no jurisdiction over

[10] Although we do not think the point is relevant to the present question, we note that, contrary to the claims of appellees (Miss. Mot. to Dismiss 17, 18) and amici (Council of the City of New Orleans Br. 5-10), FERC did consider the prudence issue in determining the appropriate allocation of the capacity and costs of Grand Gulf 1 among the four op[illegible]ing companies. FERC found (J.S. App. 115a-126a) that Grand Gulf 1 was part of a reasonable system plan to diversify the fuel base by developing nuclear power to meet anticipated growth in demand, but that the system experienced "unexpectedly dramatic" increases in the cost of the facility (*id.* at 121a). FERC also explicitly affirmed and adopted (*id.* at 122a, 146a) the findings and conclusions of its administrative law judge who determined that MSU's decisions both to begin and to complete construction of Grand Gulf 1 were prudent (see 26 F.E.R.C. at 65.112-65,113). Contrary to the claim made by amici (Council of City of New Orleans Br. 8 n.4, 9-10 n.6; APSC Br. 7 n.8), FERC's administrative law judge did not merely find that MSU officials subjectively believed that their decision to complete Grand Gulf 1 was prudent. He found that "continuing construction of Grand Gulf Unit No. 1 *was prudent* because Middle South's executives believed Grand Gulf would enable the Middle South system to diversify its base load fuel mix and, it was projected, at the same time, produce power for a total cost (capacity and energy) which would be less than existing alternatives on the system" (26 F.E.R.C. at 65,112-65,113 (emphasis added)).

The fact that no more consideration was given to the prudence issue appears to be due to the (perhaps advertent) failure of appellees and their amici to raise it. MSU introduced evidence in support of the prudence of Grand Gulf 1 in the FERC administrative proceedings. Appellees and their amici generally declined, however, to raise the issue and refute that evidence before FERC (Miss. Mot. to Dismiss App. 52-63), apparently hoping to leave the prudence issue for the state public service commissions (*id.* at 54-63). But a party cannot elude a federal agency's exclusive jurisdiction by declining to raise an issue before the federal agency.

Finally, the then-Acting Chairman of FERC did not inform Congress that "FERC did not determine prudence issues in the Grand Gulf allocation hearings" (Amicus Council of City of New

the wholesale rates charged by MSE to the operating companies. "'[T]he Supremacy Clause [does] not permit'" a state to "'usurp[] a function that Congress has assigned to a federal regulatory body'" (*Nantahala*, slip op. 10, quoting *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571, 581-582 (1981)). See generally *Arkansas Electric Coop. Corp.* v. *Arkansas Public Service Comm'n*, 461 U.S. 375, 377-380 (1983). If appellees believe that FERC's consideration of prudence was inadequate, their sole recourse is to challenge the sufficiency of FERC's determination on direct appeal or otherwise attempt to raise the prudence issue before FERC in a future appropriate proceeding regarding Grand Gulf 1. Cf. *City of Tacoma* v. *Taxpayers*, 357 U.S. 320, 339 (1958).

2. Nor is there in this case any *other* prudence inquiry, resolvable at the state level, that might allow MPSC to bar MP&L from passing through its FERC-determined share of Grand Gulf costs. Any such effort by the state would necessarily traverse matters squarely within FERC's jurisdiction.[11]

Orleans Br. 10). He stated that "the Commission did not determine the prudence of the purchase of power by the Middle South Utilities from * * * Grand Gulf." See *Powerplant Costs: Hearing Before the Subcomm. on Energy Conservation and Power of the House Comm. on Energy and Commerce*, 99th Cong., 2d Sess. 29 (1986) [hereinafter *House Hearing*]. His statement simply acknowledges that FERC's allocation did not depend on the need of an individual operating company for Grand Gulf 1 capacity (see page 23, *infra*). The Acting Chairman stressed (*House Hearing* 29), moreover, that "[n]o party raised the prudence of the purchase of power from the Grand Gulf Station as an issue in the proceedings before the Commission." The Acting Chairman elsewhere in his submission to Congress also described (*id.* at 23-24) how the preemptive effect of a FERC determination of prudence would depend "on whether the sales are individual transactions or part of an interstate power pooling arrangement, or on whether the sales are to affiliated or unaffiliated companies."

[11] Appellees' reliance (Miss. Mot. to Dismiss 16, 17 n.4) on *Pacific Gas & Electric* v. *State Energy Resources Comm'n*, 461 U.S. 190 (1983), and *Louisiana Public Service Comm'n* v. *FCC*, 476 U.S. 355

FERC exercised its exclusive jurisdiction under the Federal Power Act to review the 1982 System Agreement and the UPSA filed by MSU. FERC determined that the terms of their allocation of Grand Gulf 1 were "unjust, unreasonable, unduly discriminatory [and] preferential" (see J.S. App. 121a-123a n.18; 26 F.E.R.C. at 65,110). FERC accordingly exercised its remedial authority under Sections 205 and 206(a) of the Federal Power Act (16 U.S.C. 824d, 824e(a)) to set just and reasonable terms by ordering each of the four operating companies, including MP&L, to purchase an amount of Grand Gulf 1 capacity that would result in the companies sharing the costs of MSU's investment in nuclear generation in proportions based on their relative demand for energy on the system as a whole. On that basis, FERC allocated 33% of the power and costs of Grand Gulf 1 to MP&L. FERC's authority to impose just and reasonable obligations on the four companies was squarely affirmed by the D.C. Circuit in *Mississippi Industries* v. *FERC*, 808 F.2d at 1539-1543. The Mississippi parties—including MPSC, the Mississippi Attorney General, and Mississippi Legal Services Coalition—fully participated both in the FERC proceedings and in the review proceedings in the D.C. Circuit.

The Mississippi Supreme Court held that MPSC must, in establishing MP&L's retail rates, determine "prudence" before it permits MP&L to charge its retail customers costs it is actually bearing under FERC's order. Appellees argue that this inquiry into prudence will not invade FERC's exclusive jurisdiction. But only two sorts of prudence inquiry are logically possible: (1) whether Grand Gulf 1 was an imprudent undertaking for the

(1986), is misplaced. In the former, the Court expressly noted that FERC's "broad authority" was an exception to the states' traditional authority to regulate the need for, and pricing of, electrical generation (see 461 U.S. at 205-206). The latter decision turned on the construction of language of a federal statute not involved in this case (the Communications Act of 1934, 47 U.S.C. (& Supp. III) 151 *et seq.*).

MSU system as a whole, so that some or all of its wholesale costs should be borne by MSU's shareholders rather than by the operating companies' ratepayers, and (2) whether Grand Gulf 1 was imprudent for MP&L in some way that makes it appropriate for some or all of MP&L's share of the costs to be borne by the ratepayers of the other operating companies. There are no other possible sources of payment of MP&L's share.[12] Either inquiry would irreconcilably conflict with FERC's exclusive power over wholesale rates.

First, contrary to the suggestion of the state court (J.S. App. 18a-20a), FERC's jurisdiction to determine, for purposes of approving or adjusting MSE's wholesale rates, whether Grand Gulf 1 was a prudent undertaking for the Middle South system as a whole, obviously precludes MPSC from separately inquiring into that issue at the retail level. A state may not deem unreasonable, and hence "trap," costs incurred by a wholesaler and actually charged to the retailer in accordance with orders of FERC. The question whether MSE may charge the operating companies the full costs of Grand Gulf 1 as part of the price of the power that facility supplies to them is a question of the justness and reasonableness of the terms of interstate wholesale transactions in electric power. Once the terms of those transactions have been set, "a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A state must rather give effect to Congress's desire to give FERC plenary authority over interstate

[12] Amicus City Council of New Orleans argues (Br. 10 n.6) that MPSC could also consider whether MP&L acted imprudently in failing to sell a portion of its FERC-allocated share of Grand Gulf capacity to a third party. That argument demonstrates only desperation. First, no such inquiry is suggested by the Mississippi Supreme Court's remand to MPSC, which is confined to the issue "whether MP&L, MSE[] and MSU acted reasonably when they *constructed* Grand Gulf 1" (J.S. App. 19a-20a (emphasis added)). Second, the right to pass through FERC-determined costs obviously cannot be defeated by imagining an (evidently eleemosynary) institution willing to absorb them.

wholesale rates, and to ensure that the States do not interfere with this authority." *Nantahala*, slip op. 13.

Second, MPSC has no jurisdiction to determine that Grand Gulf 1 was imprudent for MP&L in particular in some way that makes it appropriate for more of the power and costs to be allocated to the three other utilities and their ratepayers (see J.S. App. 16a, 18a-19a). The allocation, including MP&L's 33% share, is the exact issue that FERC decided. FERC based its allocation on systemwide, interstate concerns, and intended to ensure that generating costs were shared fairly among the operating companies. FERC specifically rejected (*id.* at 172a-192a), as did the D.C. Circuit in reviewing FERC's order (see 808 F.2d at 1547-1550), the contention that the needs of individual states should dictate an operating company's just and reasonable share of Grand Gulf 1. "[T]he individual operating companies' needs are the component parts of the System power plan" and must "be subsumed by the greater interests of the entire System" (J.S. App. 184a).[13]

The D.C. Circuit expressly recognized (808 F.2d at 1548) that the direct consequence of FERC's allocation of Grand Gulf 1 capacity and costs to the four operating companies would be corresponding increases in retail rates, and squarely upheld FERC's authority to bring about that consequence (see also J.S. App. 185a-186a).

[13] The Mississippi Supreme Court also errs in focusing (J.S. App. 9a, 15a-16a) upon the amount of capacity that MP&L formally owns or to which it is entitled: all of the capacity is shared by the system as a whole, which historically has sought to roughly equalize capacity costs (see J.S. App. 121a; 30 F.E.R.C. at 65,142; 26 F.E.R.C. at 65,100). MP&L is "long" in capacity (*i.e.*, it has contributed more capacity to the system than its relative share of system demand) (see 26 F.E.R.C. at 65,103; see generally *Mississippi Industries*, 808 F.2d at 1530), but almost all of that capacity is oil and gas fired, which is the least expensive capacity on the system. Hence, if MP&L were not allocated the more expensive Grand Gulf capacity, it would bear far less of the costs of nuclear investment, and of generation generally throughout the system, than its relative share of system demand (J.S. App. 124a-125a n.19; 808 F.2d at 1564).

The suggestion that an individual state public service commission may now revisit the allocation outside the federal administrative and judicial proceedings and, in effect, veto FERC's decision is flatly contradicted by the congressional decision to provide FERC with exclusive jurisdiction over these multistate controversies.[14] As explained by the D.C. Circuit (808 F.2d at 1549 (citation and footnote omitted)), Congress concluded that FERC would be "'in the best position to reach the most equitable result and to act in the public interest, [and that the decision should not] be controlled by the necessarily parochial concerns of the States.'" See *Arkansas Electric Coop. Corp.* v. *Arkansas Public Service Comm'n*, 461 U.S. 375, 377 (1983); cf. *Public Utilities Comm'n* v. *Attelboro Steam & Electric Co.*, 273 U.S. 83, 89-90 (1927).[15]

C. *Nantahala Power & Light Co.* v. *Thornburg* Requires MPSC To Allow MP&L To Recover, In Retail Rates, Its FERC-Allocated Share Of The Costs Of Grand Gulf 1

In *Nantahala*, this Court held that "a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable" (slip op. 13). This case is not distinguishable from *Nantahala* in any relevant respect.[16]

---

[14] The Mississippi Supreme Court's reliance (J.S. App. 20a) on this Court's decision in *Western Distributing Co.* v. *PSC*, 285 U.S. 119 (1932), is misplaced. This Court did not rule in that case "that state authorities had the right, despite federal regulation, to inquire into transactions between a controlling corporation and its subsidiaries" (J.S. App. 20a). No federal regulation was involved in *Western Distributing*, which was decided in 1932, before Congress enacted Part II of the Federal Power Act in 1935.

[15] Another, related federal statute reflects this same congressional judgment. In the Public Utility Holding Company Act of 1935, Congress recognized that transactions such as these, involving subsidiar[ies] of a public utility holding company "extending over many States are not susceptible of effective control by any State" (15 U.S.C. 79a(a)).

[16] FERC's statements (J.S. App. 102a, 180a) in its federal administrative proceedings that "*Nantahala* is not directly on point"

In *Nantahala*, this Court assumed arguendo "that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*" (slip op. 19 (emphasis in original)). In *Nantahala*, the Court concluded that no such inquiry could appropriately be undertaken by the state public utility commission because FERC determined the precise amount of lower-cost power available to the utility, and "[n]o [other] source of power * * * is said to be available * * *" (*ibid.*). In this case, the Mississippi court argues (J.S. App. 16a), MPSC may determine that MP&L receives an "excessive" and "imprudent" quantity of Grand Gulf capacity under FERC's allocation because MP&L does not need the energy and there allegedly are other, lower-cost sources of energy available. The fallacy in that argument, of course, is that here, as in *Nantahala*, the *quantity* of capacity and energy to be allocated, in light of all available alternatives, is exactly what FERC determined.[17]

This is not a case of the kind envisioned in the arguendo assumption in *Nantahala*, where a utility purchases power at a FERC-approved *price* while "lower-cost power is available *elsewhere*" (slip op. 19 (emphasis added)). Rather, this is a case like *Nantahala* itself, where all of the relevant sources of power, some of which

---

and "[t]he facts of *Nantahala* are clearly distinguishable from those here" are not in point. Both statements occurred prior to this Court's decision in *Nantahala* and each referred to factual distinctions between the cases that are relevant only to a subsidiary legal issue and not to the issues in this case.

[17] In *Nantahala*, FERC allocated the benefit of low-cost power, and in this case FERC allocated the burden of high-cost power. But in each, FERC sought to ensure that each affiliated company has a mix of high and low-cost power that results in a just, reasonable, and not unduly discriminatory distribution of jointly-incurred generation costs (compare *Nantahala*, slip op. 17, with *Mississippi Industries*, 808 F.2d at 1541).

are more expensive than others, are within the utility system and the sole question—one that only FERC can fairly resolve—is how the benefits and burdens of those sources should be shared between affiliated companies doing business in different states.[18] FERC did not simply determine the reasonableness of the price of power from a particular source. Pursuant to its authority over wholesale transactions in interstate commerce, FERC determined that MP&L was obliged to bear the cost of purchasing a specified percentage of Grand Gulf 1 capacity. FERC sought to ensure that system-wide generating costs generally, and nuclear investment costs in particular, were shared among the operating companies in a just, reasonable, and not unduly discriminatory manner. On that basis, FERC specifically rejected the alternative of MP&L's purchasing less or none of that power and relying instead on lower cost sources, such as the system power pool (J.S. App. 124a n.19; 30 F.E.R.C. at 65,167; see also 808 F.2d at 1541). Hence, to paraphrase *Nantahala* (slip op. 14-15), the Mississippi court's "assertion that [MP&L] should have obtained [less] of the [high]-cost, FERC-regulated power than [MP&L] is in fact [obliged] to claim under FERC's order * * * runs directly counter to FERC's order, and therefore cannot withstand the pre-emptive force of FERC's decision." Because MP&L is not free under FERC's order to avoid that obligation by seeking out a lower-cost source of power, MPSC (and the Mississippi courts) cannot deem MP&L imprudent for failing to do so.

[18] Appellees (Miss. Mot. to Dismiss 21; MLSC Mot. to Dismiss 15-16) suggest that MP&L is somehow autonomous from the system because it formally owns certain facilities. The FERC administrative law judge rejected a similar argument advanced by AP&L (see 26 F.E.R.C. at 65,119). Those facilities are owned by MP&L, but they are part of the system's total capacity. They were "planned for and added for the benefit of the system as a whole" (*ibid.*). The Middle South system effectively determines the allocation of their capacity pursuant to system agreements, which are filed with FERC.

The Mississippi Supreme Court's mistaken reliance on the arguendo assumption in *Nantahala* stems from the court's failure to apprehend the implications for MPSC's jurisdiction of MP&L's involvement in the Middle South system. The Mississippi court treated MP&L as though it were an independent, autonomous company. FERC, however, based its allocation of financial responsibility on its finding that MP&L and the three other operating companies are all wholly-owned subsidiaries of MSU, their operations are highly coordinated and integrated, and they were all deeply involved in every aspect of the planning of Grand Gulf 1, which they intended to serve the system as a whole (J.S. App. 104a, 113a, 181a). FERC found that because of those joint efforts, the operating companies must be held jointly responsible for the cost of Grand Gulf 1, as they are for all generating costs. Contrary to the Mississippi court's assumption, they were not, FERC found, autonomous companies that could opt out of sharing in the cost of Grand Gulf 1 based on their own individual needs (*id.* at 184a-185a). See *id.* at 181a; 26 F.E.R.C. at 65,110-65,111, 65,113.

In this case, therefore, as in *Nantahala* (slip op. 15), there was no occasion for a state public utility commission to "substitute its own conception of what allocation of * * * power would have been * * * fair" on the ground that the utility should have looked "elsewhere" for power. In both cases, FERC's allocation necessarily precluded the option of looking "elsewhere." [19]

[19] The Mississippi court also suggested that MPSC "had the authority, indeed, the duty, to inquire into the prudency of the[] [UPSA and another FERC-filed system agreement]" because neither "fall[s] under the category of FERC approved rates" (J.S. App. 21a; see note 7, *supra*). The court argued that in the context of purchases by closely related entities *Nantahala* endorsed preemption only of state utility commission review of " 'FERC approved *rates*' " (J.S. App. 21a (quoting *Nantahala*, slip op. 12)). *Nantahala*, however, supports no such limitation on the preemptive scope of FERC's allocation decisions. To the contrary, the Court expressly ruled (slip op. 13 (emphasis in original)) that "the filed rate doctrine is not limited to rates *per se*." The statutory touch-

CONCLUSION

The judgment of the Supreme Court of Mississippi should be reversed.

Respectfully submitted.

CHARLES FRIED
Solicitor General

LOUIS R. COHEN
Deputy Solicitor General

RICHARD J. LAZARUS
Assistant to the Solicitor General

CATHERINE C. COOK
General Counsel

JEROME M. FEIT
Solicitor

JOHN N. ESTES III
Attorney
Federal Energy Regulatory Commission

DECEMBER 1987

---

stone for FERC's jurisdiction is whether an agreement "affects" interstate wholesale rates (see 16 U.S.C. 824e(a)). See *Mississippi Industries*, 808 F.2d at 1539-1543. In any event, any challenge to FERC's jurisdiction must be made on direct appeal of its order; FERC's jurisdiction is not subject to collateral attack in state courts.

Finally, appellees argue (Miss. Mot. to Dismiss 26-28) that MP&L should be "equitably estopped" from raising the preemption argument because MP&L allegedly espoused a contrary view of that issue in proceedings before MPSC. But whatever the power of a state regulatory body to impose disciplinary sanctions whose effect is to trap FERC-determined costs, MPSC did not purport to do so here.

☆ U. S. GOVERNMENT PRINTING OFFICE; 1987 202037 60140

AMICUS CURIAE

BRIEF

(12)

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI *ex rel.* EDWIN LLOYD PITTMAN, ATTORNEY GENERAL OF MISSISSIPPI, and MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF OF THE ARKANSAS PUBLIC SERVICE COMMISSION, MISSOURI PUBLIC SERVICE COMMISSION AND STATE OF ARKANSAS AS AMICI CURIAE IN SUPPORT OF APPELLEES

STEVE CLARK
Attorney General
MARY B. STALLCUP
Deputy Attorney General
Justice Building
Little Rock, Arkansas 72201
(501) 371-1967
Attorneys for the State of Arkansas

WALLACE L. DUNCAN
JAMES D. PEMBROKE
J. CATHY FOGEL *
JANICE L. LOWER
DUNCAN, WEINBERG, MILLER & PEMBROKE, P.C.
1615 M Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 467-6370
Attorneys for the Arkansas Public Service Commission

WILLIAM C. HARRELSON
General Counsel
PAUL H. GARDNER
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102
(314) 751-2481
Attorneys for the Missouri Public Service Commission

Dated: January 22, 1988

* Counsel of Record

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

TABLE OF CONTENTS

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI *ex rel.* EDWIN LLOYD PITTMAN,
ATTORNEY GENERAL OF MISSISSIPPI, and
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

**BRIEF OF
THE ARKANSAS PUBLIC SERVICE COMMISSION,
MISSOURI PUBLIC SERVICE COMMISSION
AND STATE OF ARKANSAS AS AMICI CURIAE
IN SUPPORT OF APPELLEES**

STATEMENT OF INTEREST OF AMICI CURIAE

The Arkansas Public Service Commission ("APSC"), State of Arkansas, and Missouri Public Service Commission ("MoPSC") (jointly "Arkansas-Missouri Parties") are vitally concerned that state regulatory commissions retain the ability to perform their statutorily-mandated obligations so that electric utilities are completely regulated. Those opposing the decision below propose remedies which would emasculate state regulatory authority and leave a substantial gap in the regulation of electric utilities.

Moreover, the Arkansas-Missouri Parties wish to address the threshold issue in this case: Whether the Federal Energy Regulatory Commission ("FERC") has jurisdiction over generating facilities and purchases of power such that it may reallocate electric power from a generating facility and require utilities to purchase additional amounts of power from that facility. If the FERC lacks such jurisdiction, there is no preemption issue to be decided in this case. The Arkansas-Missouri Parties have argued that the FERC has no such jurisdiction in *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir.), *reh'g granted and vacated in part*, 822 F.2d 1104 (D.C. Cir. 1987), *cert. denied sub nom. Arkansas Public Service Comm'n v. FERC*, 56 U.S.L.W. 3412 (Dec. 15, 1987), *aff'g Middle South Energy, Inc., and Middle South Services, Inc.*, Opinion No. 234, 31 FERC (CCH) ¶ 61,305 (1985) ("Opinion No. 234"); App. 73a-152a and *Middle South Energy, Inc., and Middle South Services, Inc.*, Opinion No. 234-A, 32 FERC (CCH) ¶ 61,425 (1985) ("Opinion No. 234-A"); Appendix to Jurisdictional Statement, 153a-195a ("J.S. App."). There, the FERC ordered the Arkansas Power & Light Company ("AP&L") to purchase 36% of the Grand Gulf nuclear power plant ("Grand Gulf") and thereby imposed upon Arkansas and Missouri ratepayers approximately 3 billion additional dollars in electric rates in the next ten years and substantially more for the life of the plant.

SUMMARY OF ARGUMENT

The instant case is moot because the FERC lacks jurisdiction to reallocate generating facilities. Therefore, the action of the court below was proper, because the Supremacy Clause of the United States Constitution, U.S. Const., Art. 6, Cl. 2, does not prohibit state action where no federal jurisdiction exists. Pursuant to its grant of authority in the Federal Power Act, 16 U.S.C. § 824 (1982), the FERC may only regulate generating facilities in specified situations. The Federal Power Act does not allow the FERC to reallocate the amount of generating capacity which utilities may purchase. Additionally, the Federal Power Act does not allow the FERC to regulate purchases of electric power or to interfere with state regulatory authority. *See* 16 U.S.C. § 824 (1982). Since the FERC lacked the authority to act as it did, no issue is joined regarding the interplay of state and federal regulatory authority in this transaction and no Supremacy Clause question is presented.

In deciding Opinion No. 234, the alleged source of the Supremacy Clause conflict herein, the FERC regulated generating facilities in a manner not permitted pursuant to the Federal Power Act, required utilities to purchase electric power against their will, even though the Federal Power Act does not grant FERC jurisdiction over purchasers, and prevented effective state regulation of electric utilities. Moreover, by forcing utilities to purchase unwanted power, the FERC essentially precluded any regulatory agency from determining whether the decision by individual operating companies to purchase that power was prudent. The ultimate purchase decision was not that of the utility, but that of the FERC. The Federal Power Act was enacted to close, not to reopen, a regulatory gap.

Because the decision of the FERC was beyond its jurisdiction, it is void. Therefore, the Mississippi Public Service Commission has the jurisdiction to examine the rates of Mississippi Power & Light Company ("MP&L") without violating the Supremacy Clause.

INTRODUCTORY STATEMENT

MP&L, appellant herein, contends that the Mississippi Public Service Commission has no jurisdiction to investigate the costs of Grand Gulf. Relying upon *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986), MP&L claims that the FERC has reallocated the amount of Grand Gulf capacity to be sold to operating companies of Middle South Utilities ("MSU"), and through the

operation of the Supremacy Clause of the United States Constitution, a flowthrough of the costs[1] ordered by the FERC is required. This argument is based upon the assumption that the FERC had jurisdiction to reallocate Grand Gulf and that, therefore, the Supremacy Clause attaches.

However, the FERC lacks jurisdiction to reallocate Grand Gulf. It is this threshold issue—FERC jurisdiction to reallocate Grand Gulf—which must be decided before any decision can be made regarding the applicability of the Supremacy Clause. The Arkansas-Missouri Parties take no position herein as to the applicability of *Nantahala* to the decision below if this Court determines that the FERC had jurisdiction to reallocate Grand Gulf.

FACTUAL BACKGROUND

MSU is a public utility holding company with four operating company subsidiaries: AP&L, Louisiana Power & Light Co. ("LP&L"), MP&L and New Orleans Public Service, Inc. ("NOPSI"). MSU also owns MSE, a generating subsidiary which owns a single power plant: Grand Gulf.

Grand Gulf was constructed, in part, to allow the MSU operating companies to diversify their fuel source. *See* Opinion No. 234, 31 FERC (CCH) at 61,651-53; J.S. App. 115a-118a. MSU operating companies agreed to purchase Grand Gulf power pursuant to a Unit Power Sales Agreement ("UPSA") in the following proportions:

[1] Grand Gulf is nominally owned by System Energy Resources, Inc., the new name of Middle South Energy, Inc. ("MSE"). MSE, in turn, sells Grand Gulf power to the MSU operating companies. Therefore, the activity involved is a "sale at wholesale" by MSE and thus jurisdictional before the FERC. The purchase of Grand Gulf power is part of the costs incurred by MSU operating companies. This contrasts with normal power plant ownership in which the cost of a power plant is part of a utility's rate base. *See* p. 11, *infra*. To the extent there is no arms length transaction, there is no "sale" at wholesale and therefore no FERC jurisdiction.

	Percentage	MW
LP&L:	38.57%	434
MP&L:	31.63%	356
NOPSI	29.80%	335
AP&L:	0%	0

See Mississippi Industries v. FERC, 808 F.2d 1525, 1554 (D.C. Cir. 1987). On June 18, 1982, MSE tendered for filing with the FERC the UPSA. *See Middle South Energy, Inc.*, Docket No. ER82-616-000 (filed June 18, 1982).

MSU operating companies coordinate their power pooling activities pursuant to a System Agreement, the latest of which, the 1982 System Agreement, was filed with the FERC on April 30, 1982. *See Middle South Services, Inc.*, FERC Docket No. 82-483-000 (filed April 30, 1982). In a consideration of these two filings,[2] the FERC rejected the allocation of Grand Gulf power included in the UPSA among the MSU operating companies and, instead, required the MSU operating companies to accept the following allocation:[3]

	Percentage	MW
LP&L:	14%	158
MP&L:	33%	371
NOPSI	17%	191
AP&L:	36%	405

See Opinion No. 234, 31 FERC at 61,655; J.S. App. 123a. This allocation is not based upon the need for power of

[2] The FERC assigned Middle South Energy, Inc., and Middle South Services, Inc., to separate Presiding Administrative Law Judges, who issued separate opinions. *See* Middle South Energy, Inc., 26 FERC (CCH) ¶ 63,044 (1984); Middle South Services, Inc., 30 FERC (CCH) ¶ 63,030 (1985). Although the FERC never consolidated the two cases formally, it issued a single opinion on the two cases. *See* Opinion No. 234.

[3] This allocation was initially adopted by the Presiding Administrative Law Judge in Middle South Energy, Inc., 26 FERC at 65,119.

any of the operating companies, or upon the demand for power of those companies. Rather, the FERC examined the investment made by each operating company in nuclear power plants and equalized that investment using Grand Gulf as a surrogate. The calculation involved three nuclear power plants in addition to Grand Gulf: Waterford 3, a high cost nuclear power plant owned solely by LP&L, and ANO 1 and 2, two low cost nuclear power plants owned by AP&L. The net effect was to displace state regulation over these three other nuclear plants. As a result of the FERC decision, AP&L, which had built two nuclear and four coal units to meet native load, and which had agreed to purchase no Grand Gulf power, was required to purchase 36% of Grand Gulf.

ARGUMENT

The FERC has no jurisdiction to reallocate Grand Gulf, because the Federal Power Act specifically prohibits FERC from exercising jurisdiction over generating facilities unless speeifically provided in the Act, limits FERC authority to matters not regulated by the states, and fails to grant FERC jurisdiction to order the purchase of power. *See* 16 U.S.C. § 824 (1982). Determining that FERC has jurisdiction would result in a substantial regulatory gap.

The FERC Lacks Jurisdiction over Generating Facilities

The Federal Power Act specifically prohibits FERC regulation of generation except in limited circumstances.[4] When it enacted the Federal Power Act, Congress did not grant the FERC jurisdiction over generating facilities, because Congress wished to retain effective state control over these facilities in order to allow continued effective state regulation of electric utilities.

[4] *See* note 6, *infra*.

In the development of the Federal Power Act, the Senate bill specifically gave the Commission authority to regulate "the production of electric energy" and the "facilities for such production." *See* S. 2796, 74th Cong., 1st Sess. (1935). Senate Bill No. 2796 specifically excluded from Commission jurisdiction "the retail sale of such energy in local distribution." The Chairman of the jurisdictional Senate Committee on Interstate Commerce stated in floor debate that the legislation, in that early form, would exclude jurisdicion over production facilities in intrastate commerce but would include jurisdiction over such facilities in interstate commerce. *See* 79 Cong. Rec. 8431 (1935). In other words, the Senate bill, as drafted, would have allowed the FERC to do precisely what it did in Opinion No. 234: reallocate generating facilities relying on the effect of the generating facilities on wholesale sales in interstate commerce.

However, the Senate bill was never adopted. The House bill specifically *prohibited* any Commission regulation of generating facilities. *See* S. 2796 as reported by the House Committee on Interstate and Foreign Commerce. *See also* H.R. Rep. No. 1318, 74th Cong., 1st Sess. at 26-27 (1935):

As ultimately adopted, the Act provides:

> The Commission . . . shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy. . . .

16 U.S.C. § 824(b)(1); J.S. App. 62a. Although there are specific provisions in the Federal Power Act providing for FERC jurisdiction over generating facilities,[5] noth-

[5] The following sections of Parts II and III of the Federal Power Act *specifically* provide for Commission regulation regarding generating facilities: Section 202(a), 16 U.S.C. § 824a(a) ("Commission is empowered and directed to divide the country into regional districts for the voluntary interconnection and coordination of facili-

ing in the Act allows the FERC to reallocate generating facilities.

Such limited jurisdiction over generating facilities reflects a second goal of the Federal Power Act: the limitation of FERC regulatory authority "to those matters which are not subject to regulation by the States." *See* 16 U.S.C. § 824(a) (1982); J.S. App. 62a. Traditionally, states have regulated generating facilities. Both the House and Senate, in considering the Federal Power Act, expressed concern that the Act not limit existing state regulatory authority. For example, the Senate Report stated:

> [Section 201(a)] also declares the policy of Congress to extend that regulation to those matters which cannot be regulated by the States and to assist the States in the exercise of their regulatory

---

ties for the generation, transmission, and sale of electric energy . . ."); Section 202(c), 16 U.S.C. § 824a(c) (during war or other emergency, Commission may "require by order such temporary connections of facilities and such generation, delivery, interchange, or transmission of electric energy as in its judgment will best meet the emergency and serve the public interest."); Section 206(b), 16 U.S.C. § 824e(b); J.S. App. 67a-68a (Commission "may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy."); Section 208, 16 U.S.C. § 824g ("Commission may investigate and ascertain the actual legitimate cost of the property of every public utility, the depreciation therein, and . . . other facts which bear on the determination of such cost or depreciation, and the fair value of such property"; public utilities must file inventory of property and original cost thereof); Section 302(a), 16 U.S.C. § 825a(a) (Commission may determine rates of depreciation for utility property); Section 304, 16 U.S.C. § 825c (public utilities and licensees must file reports and Commission may order that reports include information on cost of generation); Section 311, 16 U.S.C. § 825j (Commission may conduct investigations regarding generation in order to secure information for recommending legislation).

> powers, but not to impair or diminish the powers of any State commission.

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). Similarly, the House Report stated:

> The bill takes no authority from State commissions. . . . The new parts are drawn as to be a complement to and in no sense a usurpation of State regulatory authority. . . . Probably, no bill in recent years has so recognized the responsibilities of State regulatory commissions as does title II of this bill.

H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

The decision by the House of Representatives to deny jurisdiction over generating facilities was based in large part upon its concern that such jurisdiction would undermine state regulatory authority. Representative Cole, a member of the Committee that reported the Federal Power Act, described the generating facilities provision in the Senate bill which was ultimately rejected:

> Title II, as it passed the Senate, applied to not only the transmission and sale of electric energy in interstate commerce but to the production and generation thereof. The bill, furthermore, ignored in many ways not only the prerogatives but the existing regulatory provisions by the States of certain activities covered therein.

79 Cong. Rec. 10383-84 (1935). Thus, the rejection of the Senate bill and the ultimate denial of Commission jurisdiction over generating facilities in the Federal Power Act was in large part based upon the need to assure effective state regulation of electric utilities.

Normally, a state is able to regulate jurisdictional utilities in matters regarding generation because it has specific statutory authority and responsibility to do so and may, therefore, review actions by utilities in generation planning before generating plants are authorized, review the reasonableness of the methods proposed to ef-

fect generating plant construction and operation, and review the result of generating plant construction and operation to ensure that the costs actually incurred in achieving those results were reasonable.[6] State regulatory commissions accomplish these goals in large part by examining the propriety of expenditures by a utility for generation construction, which many times constitutes more than half of total utility costs.

A utility would have two different ways of obtaining generation capacity: purchase or ownership. With regard to the purchase option, normally a utility will purchase all or part of its requirements for electric power from another operating utility either through coordination transactions or requirements service.[7] These transactions involve a purchase of a portion of all generation on the system of the selling utility but do not guarantee

[6] APSC and MoPSC have the duty to assure that the retail rates of AP&L are just and reasonable. In addition, public utilities in Arkansas, including AP&L, are required to apply to the APSC for approval of other operations, including construction of generating facilities, pursuant to Ark. Code Ann. 23-18-501 through 23-18-508 (1987) (codifying Act 164 of 1973, as amended); issuance of stocks, bonds or other evidences of indebtedness or creation of liens against utility property in Arkansas, pursuant to Ark. Code Ann. 23-3-103 and 23-3-104 (1987); and the purchase, sale, lease, or rent of any utility property constituting an operating system or unit, pursuant to Ark. Code Ann. 23-3-102 (1987). Similarly, in Missouri, the MoPSC may, in ordinary circumstances, exert authority over the construction or operation of plants in Missouri through its authority to approve all issuances of stock, bonds, notes or other evidences of indebtedness payable at periods of more than twelve months; and approve any sale, lease, transfer, mortgage, disposition, encumbrance, merger or consolidation of all or any part of its franchise, works or system. *See* Mo. Rev. Stat. §§ 393.170, 393.190, 393.200 (1978).

[7] The FERC has identified coordination transactions and requirements service as the two major types of jurisdictional wholesale transactions involving generation. *See* Regulation of Electricity Sales for Resale and Transmission Service (Phase I), FERC Statutes and Regulations (CCH) ¶ 35,518 (1985).

the purchaser a right to the output of any single generating unit.

With regard to ownership, there are two traditional methods of acquiring the output of a specific generating unit. First, and most simply, a utility may own a generating unit to be used solely for its own benefit. Second, a generating unit may be jointly owned by more than one utility.

A unit power sale, such as provided for in the UPSA, is a hybrid where one utility sells all or a portion of the output of a specific generating unit to other utilities. It is not quite ownership, although it essentially amounts to ownership because the purchasing utilities pay the entire cost of the power plant and receive the entire amount of power produced by the power plant over the life of the power plant or for a term certain. *See Otter Tail Power Company v. Federal Power Comm'n*, 473 F.2d 1253 (8th Cir. 1973). A unit power sale is deemed a "wholesale sale" because one entity—the entity owning the generating plant—sells the output of a generating unit to utilities for resale to ultimate consumers. Yet, the unit power sale is different from the normal wholesale sale which is made by one operating utility to another operating utility, because the unit power sale guarantees to the purchasing utility a portion of the output of a specific generating plant. In a unit power sale, the selling entity may be, as in the case of MSE, a corporation whose sole function is to own a generating facility, the output of which is sold through unit power sales. Although MSE served as a financing mechanism for Grand Gulf, such a generating subsidiary could be totally a paper corporation, whose sole function is to change what would be a joint ownership situation to a wholesale sale.

Where a utility owns a generating unit, either individually or jointly, there is no question that the jurisdictional state regulatory agency may, pursuant to appli-

cable state law, review the propriety of the decision to construct or purchase the power plant, the prudence of continuing construction of the power plant, the appropriateness of expenditures made in constructing the power plant, and, ultimately, the amount of the cost of the power plant which must be paid by ratepayers and the amount which must be paid by shareholders. Where a utility purchases power at wholesale, the FERC determines the appropriate wholesale rate to be paid and a state regulatory commission may not recalculate it,[8] with the state commission's authority arguably being limited to a determination whether a utility acted imprudently by choosing to purchase power at wholesale from a particular source.[9] By regulating the prudence of expenditures, either of ownership or of purchase, a state regulatory commission may fulfill its duty to assure ratepayers of just, reasonable, and nondiscriminatory rates.

On the federal side, the FERC also plays a very important role in utility ratemaking. It examines a utility's cost of service to assure that wholesale rates are just, reasonable, and not unduly discriminatory. *See* 16 U.S.C. §§ 824d and 824e; J.S. App. 63a-67a. When the FERC determines the appropriate wholesale rate per kilowatt and per kilowatt-hour, it is not infringing upon the ability of the retail commission to set retail rates as long as that retail commission retains the ability to regulate the prudence of any purchase or construction.

When the FERC alters the amount of power purchased, however, it undermines the ability of a state commission to regulate generating facilities and determine prudence

[8] *See* Nantahala Power & Light Co. v. Thornburg, 476 U.S. 953 (1986).

[9] *See* Appeal of Sinclair Machine Products, Inc., 126 N.H. 822, 498 A.2d 696 (1985); Pike County Light & Power Co.—Electric Division v. Pennsylvania Public Utility Comm'n., 77 Pa. Comm'w. 268, 465 A.2d 735 (1983).

of purchase since FERC has improperly assumed the authority to determine what portion of a generating plant must be purchased by various utilities.[10] For example, through Opinion No. 234, the FERC has eliminated the effectiveness of past and future regulation by the APSC of new generating facilities and appropriate rates for AP&L. As part of its regulatory role, the APSC approved the construction of many power plants constructed by AP&L, including two nuclear power plants, ANO 1 and 2, and four coal plants because such facilities were needed for Arkansas consumers. *See Middle South Services, Inc.*, 30 FERC (CCH) ¶ 63,030 at 65,162 (1985). In Opinion No. 234, the FERC has undermined that determination and removed low cost facilities from AP&L by effectively forcing a sale from those facilities to consumers in Louisiana and Mississippi. Further, the APSC and MoPSC have traditionally examined the costs and rate base of AP&L to assure Arkansas and Missouri consumers of just and reasonable rates. In Opinion No. 234, the FERC determined that the costs of two major and expensive nuclear power plants—Grand Gulf No. 1 and Waterford No. 3—would be effectively rate based to AP&L retail customers and must be charged as costs to AP&L.

In short, the FERC has undermined the ability of the state commissions to regulate effectively any power company subject to a FERC reallocation order. In so doing, the FERC, perhaps unwittingly, has created the ability in utilities to evade federal or state jurisdiction by forming or dissolving generation subsidiaries. By forming a generation subsidiary, a utility may obtain federal and evade state jurisdiction because a generation subsidiary, at least in form, sells electric power at wholesale. By dissolving a generation subsidiary, a company may evade federal and obtain state jurisdiction because the ownership of generation is beyond the FERC's jurisdiction.

[10] Prudence of purchase is discussed at p. 15-18, *infra*.

By reallocating Grand Gulf power, and, effectively, Waterford 3 and ANO 1 and 2, the FERC has not merely impaired or diminished state regulatory authority. It has dramatically usurped such authority. Such utilization of the Federal Power Act to reallocate the output of generating plants, with the result that these four plants will be subject to federal, rather than state, rate regulation violates the clear terms of the Federal Power Act and totally distorts the intent of the framers of the Federal Power Act to retain extensive state jurisdiction and to prohibit FERC regulation of generating facilities.

The FERC Lacks Jurisdiction Over Purchases of Power

While the FERC has specific authority over the sale of electric energy at wholesale pursuant to Section 201 of the Federal Power Act, 16 U.S.C. § 824 (1982); J.S. App. 62a-63a, it has no such jurisdiction over the purchases of electric power. Nowhere in the Federal Power Act is the FERC granted jurisdiction over such purchases, and Commission jurisdiction over purchases may not be implied from its jurisdiction over sales. Yet FERC, in its Orders 234 and 234-A, has asserted jurisdiction over the purchase of power from Grand Gulf by AP&L, LP&L, MP&L and NOPSI.

A number of courts, including this Court, have implied that the FERC has jurisdiction over sellers, but not purchasers of electric energy in interstate commerce. They have done so in cases involving Commission jurisdiction over transactions involving an entity exempt under Section 201(f), 16 U.S.C. § 824(f) (1982), and have concluded that the FERC always has jurisdiction over such transactions where the seller is a jurisdictional entity even if the buyer is an exempt entity [11] but never

---

[11] *See* United States v. Public Utilities Comm'n of the State of California, 345 U.S. 295, 312-15 (1953); California Electric Power Co. v. FPC, 199 F.2d 206 (9th Cir. 1952), *cert. denied,* 345 U.S. 834 (1953); Wisconsin-Michigan Power Co. v. FPC, 197 F.2d 472, 479 (7th Cir. 1952), *cert. denied,* 345 U.S. 934 (1953).

has such jurisdiction where the seller is an exempt entity.[12] As the court stated in *California Electric Power Co.*: "The entire thrust of Part II is toward the seller at wholesale, not the buyer." 199 F.2d at 208-09.

The FERC has previously determined that it lacks authority to require an entity to purchase power from another. *See Southern Company Services, Inc.*, 20 FERC (CCH) ¶ 61,332 (1982). The Federal Power Act has not been amended to grant it such authority. The FERC has implied that its actions in Opinion No. 234 may well constitute a forced purchase and sale.[13] In such a case, the FERC has no jurisdiction to reallocate Grand Gulf power, thus forcing a purchase of power.

The FERC's Decision Creates a Regulatory Gap

An analysis of FERC's decisions regarding its jurisdiction reveals a significant gap in its regulation of hold-

---

[12] *See* United States v. Public Utilities Comm'n of the State of California, 345 U.S. at 313, n.23.

[13] *See* Middle South Energy, Inc., and Middle South Services, Inc., Opinion No. 234-A, 32 FERC at 61,948-49; J.S. App. 164a-167a. Although the FERC claimed in Opinion No. 234 that the issue was not forced purchase or sale "but rather is the appropriate costs ALLOCATION OF among integrated companies owned by the same parent," 31 FERC at 61,643; J.S. App. 101a, the FERC in the instant case makes clear that its order in Opinion No. 234 forced MSU operating companies to purchase Grand Gulf power. *See* Brief for the United States and the Federal Energy Regulatory Commission as Amici Curiae at 1, 13, 21, 26, Mississippi Power & Light Co. v. State of Mississippi, No. 86-1970. In Opinion No. 234, the FERC claimed to have jurisdiction because the transaction constituted a jurisdictional wholesale sale. It also claimed to have reallocated Grand Gulf power on the basis that MSU is a highly integrated company. The FERC cannot have it both ways. If the UPSA is a jurisdictional wholesale sale, the FERC order resulted in a forced purchase, which is beyond FERC authority. If it is an intra-company transaction as a result of MSU's highly integrated nature, no sale occurred, and therefore, the FERC lacks jurisdiction over the transaction.

ing companies. A reversal of the decision below will give that regulatory gap continued existence.

The FERC has consistently declined to regulate the prudence of power purchases except in one, very limited situation which is not apposite here.[14] Although the FERC has guardedly asserted that it may review prudence in the context of a holding company situation,[15] a careful examination of its claim indicates that FERC believes itself limited to examining prudence in the context of cost allocation and pool agreement interpretation. *See AEP Generating Co.*, 36 FERC (CCH) ¶ 61,226 at 61,550 (1986). Thus, the FERC apparently considers itself jurisdictionally able to examine prudence of the interrelationship of pool members but considers itself jurisdictionally unable to impose upon stockholders, rather than ratepayers, the costs of imprudent decisions by a single operating company in a holding company. Rather, the FERC believes that it may impose imprudent costs upon stockholders only where the holding company itself was imprudent in making a decision to construct a power plant. *See AEP Generating Co. and Kentucky Power Co.*, 38 FERC (CCH) ¶ 61,243 at 61,812, 61,825 n.5 (1987).

Further, the FERC asserts that it may not determine whether a utility should have purchased power from an alternative supplier or should have engaged in conservation activities to limit the need for new power sources. *See Monongahela Power Co., et al.*, 39 FERC (CCH) ¶ 61,350 at 62,098 (1987). Additionally, while admitting that it lacks jurisdiction over the licensing of generation

[14] The FERC will review the prudence of a power purchase insofar as the purchase is an expense item in a wholesale selling company's rates. *See* Southern Company Services, Inc., 28 FERC (CCH) ¶ 61,349 (1984); Pacific Power & Light Co., 27 FERC (CCH) ¶ 61,080 at 61,148 (1984); Pennsylvania Power & Light Co., 23 FERC (CCH) ¶ 61,325 at 61,716 (1983).

[15] *See* AEP Generating Co., 36 FERC ¶ 61,226 at 61,550 (1986).

facilities, the FERC asserts that it may not order a utility to construct a facility or to conserve energy in order to effect a proposed power supply plan. *See id.* The FERC further asserts that neither it nor a state regulatory commission has the ability to determine whether a single operating company should have entered into a holding company pooling agreement, that jurisdiction residing in the Securities and Exchange Commission. *See American Electric Power Service Corp.*, 32 FERC ¶ 61,363 at 61,818, 61,819 n.4 (1985). Finally, the FERC has claimed that a state utility commission must recognize a FERC-approved rate in fixing retail rates.[16]

As a result of the FERC assertion of exclusive federal jurisdiction in the area of holding company operations,[17] the operating company members of holding companies would be unregulated to a great degree regarding prudence of purchases whenever the FERC reallocates power among such operating companies. No regulatory agency would be able to determine whether the power purchase, rather than an alternative purchase, is appropriate. No regulatory agency with expertise in electric utility matters would be able to determine whether participation in a power pooling agreement is prudent. Further, no regulatory agency would be able to determine whether the purchase of power from a facility the FERC

[16] *See* Kentucky Power Co., 36 FERC (CCH) ¶ 61,227 at 61,554 (1986). At least one federal appellate court has recognized the difficulty in arguing before any state commission that AP&L made an imprudent purchase of Grand Gulf power where AP&L did not choose to buy Grand Gulf power but, rather, was forced by the FERC to do so. *See* Arkansas Power & Light Co. v. Missouri Public Service Comm'n, 829 F.2d 1444, 1450 n.4 (8th Cir. 1987).

[17] The jurisdiction of the Securities and Exchange Commission focuses on a review of the propriety of continued membership in the holding company by one of its constituent members. *See* American Electric Power Service Corp., 32 FERC (CCH) at 61,319, n.4.

has reallocated was a prudent action of the individual operating company.

As a result, the AP&L management and MSU stockholders may not be held responsible for the purchase of Grand Gulf power rather than power from another source or conservation of power, and the ratepayers must bear the cost of such purchase. The APSC and MoPSC would likely have approved of the decision of AP&L management to refrain from such purchase. Now, they may be constrained from judging the prudence of purchase of such power, and, since FERC does not regulate the prudence of purchase, a regulatory gap exists resulting in no review in the prudence of the Grand Gulf purchase.

There are at least two essential components to effective regulation of electric utilities. One is to ensure that rates are computed properly and that ratepayers do not pay an excessive amount for utility services based upon a utility's rate base and incurred costs. The second, and perhaps more important component, is to assure that costs are minimized through efficient management decisions. This second component of ratemaking is lost where, as here, AP&L may recover all of Grand Gulf's costs because regulators are precluded from examining prudence of purchase.

As this Court has determined, the Federal Power Act was enacted to eliminate a regulatory gap. *See Federal Power Comm'n v. Southern California Edison Co.*, 376 U.S. 205, 213-14 (1964). This Court should not allow the FERC to create a new regulatory gap, thereby undermining the purpose of the Federal Power Act.

CONCLUSION

For the foregoing reasons, the Arkansas-Missouri Parties urge this Court to dismiss the instant case as moot on the grounds that the Federal Power Act did not grant authority to the FERC to issue the reallocation decision in Opinion Nos. 234 and 234-A and that, therefore, no Supremacy Clause issue may arise because there will be no federal conflict with the exercise of state regulatory authority.

Respectfully submitted,

STEVE CLARK
Attorney General
MARY B. STALLCUP
Deputy Attorney General
Justice Building
Little Rock, Arkansas 72201
(501) 371-1967
Attorneys for the State of Arkansas

WALLACE L. DUNCAN
JAMES D. PEMBROKE
J. CATHY FOGEL *
JANICE L. LOWER
DUNCAN, WEINBERG, MILLER & PEMBROKE, P.C.
1615 M Street, N.W.
Suite 800
Washington, D.C. 20036
(202) 467-6370
Attorneys for the Arkansas Public Service Commission

WILLIAM C. HARRELSON
General Counsel
PAUL H. GARDNER
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102
(314) 751-2481
Attorneys for the Missouri Public Service Commission

* Counsel of Record

Dated: January 22, 1988

AMICUS CURIAE

BRIEF

86 1970

IN THE SUPREME COURT OF THE UNITED STATES
October Term 1987

MISSISSIPPI POWER & LIGHT, Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN, Attorney General and MISSISSIPPI LEGAL SERVICES COALITION, Appellees

On Appeal from the Supreme Court of Mississippi

BRIEF FOR CONSUMER FEDERATION OF AMERICA, ENVIRONMENTAL ACTION, AND CITIZEN/LABOR ENERGY COALITION

Scott Hempling
Counsel of Record

Environmental Action Foundation
1525 New Hampshire Ave.
Washington, DC 20036
(202) 745-4871

Of counsel:
Roger Colton
72 Maple St.
Belmont, MA 02178

January 22, 1988

TABLE OF CONTENTS

TABLE OF AUTHORITIES

COURT CASES

AGENCY CASES

STATUTES

INTEREST OF AMICI CURIAE

Consumer Federation of America ("CFA"), a non-profit organization founded in 1968, is the nation's largest consumer advocacy organization. CFA's membership encompasses more than 200 national, state and local consumer, senior citizen, low-income, union, farm, labor, public power and cooperative organizations representing more than 35 million people.

Environmental Action ("EA") is a non-profit, environmental research and education organization based in Washington, D.C., with members located throughout the United States. EA's major work focuses on energy, toxic waste and solid waste.

Citizen/Labor Energy Coalition ("C/LEC"), founded in 1978, is a coalition of labor, citizen, religious and community organizations working on energy issues affecting low and moderate income groups.

Collectively, amici represent consumers

of electricity and residents of communities affected by power plant construction. These consumers and residents seek to ensure that regulatory treatment of investor-owned utility companies, and particularly treatment of these companies' power plant construction decisions, is responsive to consumer, community and environmental concerns.

SUMMARY OF ARGUMENT

State inquiry into the prudence of an affiliate of a multistate holding company will not interfere with decisions of the Federal Energy Regulatory Commission ("FERC") correcting discrimination among all four affiliates of that holding company. The issues of prudence and cost allocation are logically distinct. As a result, the State of Mississippi should be free to investigate whether Mississippi Power & Light ("MP&L") could have managed

its off-system purchases and load management practices in such a manner as to reduce its 33% FERC-assigned share of Grand Gulf costs. Moreover, nothing in FERC's allocation decision precludes Mississippi from inquiring into MP&L's current and future efforts to ease the impact on its customers caused by the FERC allocation.

This Court's decision in Nantahala Power & Light Co. v. Thornburg, 106 S.Ct. 2349 (1986), assumed that only on-system power was available to the buying utility. Nantahala does not preclude state prudence review where off-system sources, or their load management equivalents, are available.

In 1974, MP&L and Middle South Energy ("MSE") sought a Certificate of Convenience an Necessity ("CCN") from the Mississippi Public Service Commission ("MPSC") to build Grand Gulf. The MPSC conditioned the CCN on MP&L and MSE accepting the risk that Grand Gulf would prove uneconomic or

excessively large. If States may bar a utility affiliation outright, they certainly may condition that affiliation on utility acceptance of risk. MP&L and MSE may not use the holding company structure, along with the Federal Power Act, to avoid that risk.

Finally, FERC preemption should not apply where the buying utility has financial independence from the selling utility. The requirements of filed rate doctrine are fulfilled when the seller receives his FERC-filed rate. What happens to the buyer at the hands of duly enacted state standards is of no legitimate concern to FERC.

ARGUMENT

I. FERC'S DUTY TO CORRECT DISCRIMINATION AMONG AFFILIATES DOES NOT PREEMPT STATE PRUDENCE REVIEW OF EACH INDIVIDUAL AFFILIATE

MP&L, FERC and EEI generally assert

that the orders of the Federal Energy Regulatory Commission ("FERC") allocating Grand Gulf costs among the four operating subsidiaries of Middle South Utilities ("MSU") preempt the State of Mississippi from questioning the actions of Mississippi Power & Light ("MP&L"). As discussed below, there is no grounds for preemption. Mississippi's exercise of its traditional powers of prudence review will not interfere with FERC's efforts to correct discrimination on the Middle South system. Furthermore, this Court's decision in Nantahala Power & Light Co. v. Thornburg, 106 S.Ct. 2349 (1986), assumed that only on-system power was available to the buying utility; therefore, Nantahala does not preclude prudence review where off-system sources, or their load management equivalents, may be available.

Finally, MP&L's suggestion that FERC's decision amounts to a regional power plan

that must override contrary state plans inaccurately describes FERC's decisions and assumes powers which FERC does not have.

A. Mississippi's Review of MP&L's Prudence Will Not Interfere With FERC's Correction of MSU's Discrimination

In setting wholesale rates among the subsidiaries of a multistate holding company, FERC's duty is to guard against intercompany discrimination. Mississippi's duty is to assure that MP&L, beneficiary of the state-granted monopoly franchise, behaves consistently with the obligations accompanying that franchise. The inquiries necessary to carry out these duties are logically distinct. Even as FERC allocates 33% of Grand Gulf to MP&L, two types of prudence questions surface: (1) Could MP&L, in the 1970's, have behaved in a manner that would have reduced the share of Grand Gulf it ultimately received? (2) Is MP&L now taking appropriate action to

reduce the burden caused by its share? Answering these questions at the state level will cause no interference with FERC's orders.

1. The Issues of Prudence and Cost Allocation Are Logically Distinct

A prudence inquiry protects customers from the negligence of company managers. The regulator must explore "the particular circumstances existing either at the time the challenged costs were actually incurred or the time the utility became committed to incur those expenses." New England Power Co., 31 F.E.R.C. para. 61,047 at p. 61,084 (1985).

Intracompany cost allocation is a different matter altogether. In the context of Grand Gulf and the Middle South system, FERC's goal was to define each operating subsidiary's responsibility for system costs. The purpose is to insulate each subsidiary from the responsibilities

of its sister companies.

The intent behind the Middle South system agreements confirms this clear distinction between prudence and allocation. The 1973 and 1982 cost-sharing agreements on the Middle South system label each operating subsidiary "long" or "short," and devise methods to arrive at a rough equalization of system costs. The concepts of "long" or "short" in the System Agreements do not bear any relation to the needs of any particular company. Rather, these concepts concern whether the share of total system capacity which a particular company owns is more or less than that company's share of total system demand. All capacity is allocated to someone, regardless of prudence or need. The clear purpose of these allocation provisions thus cannot be to assure prudent power planning, but to assure MSU that all excess capacity will be "soaked up" by some company.

FERC now has approved, with modifications, Middle South's method for distributing excess capacity on the system. But two types of questions remain as to whether MP&L could have reduced, or can in the future reduce, the costs associated with its allocated share of this excess. These two areas are discussed below.

2. FERC's Post-1982 Cost Allocation Cannot Double As a Finding on MP&L's Pre-1982 Prudence

a. MP&L's Pre-1982 Imprudence May Have Caused Its Post-1982 Cost Burdens

In 1974, when MP&L sought and obtained MPSC authorization to commit to Grand Gulf, MP&L was party to the 1973 System Agreement. Like the 1982 Agreement, the 1973 Agreement assigned system excess capacity to each company according to its

relative "shortness" or "longness." [1] The 1973 Agreement also granted certain flexibility to the operating companies. For example, Section 1.01 permitted any company to terminate its participation on 48 months written notice. Section 4.02 permitted any company, with the consent of the Operating Committee, to purchase power and energy off-system. The Agreement placed no restrictions on each company's inherent ability to reduce its customers' demand through load management techniques.

Having committed to Grand Gulf, MP&L thus confronted a situation where it could manage its growth during the 1970's in a manner that would minimize its responsibility for future system excess capacity costs. For example, was MP&L's

---

[1] Under both the 1973 and 1982 System Agreements, each operating subsidiary is allocated a share of system capacity costs roughly in proportion to that subsidiary's share of system demand. See J.S. App. at 84a.

power supply planning and load management in the 1970's prudent, given the pressures created and flexibility provided by the 1973 System Agreement? Moreover, if MP&L was imprudent, did this imprudence place MP&L in a position of relative "shortness," leaving it vulnerable to the 33% allocation ultimately ordered by FERC?

FERC has held that in proceedings concerning the justness and reasonableness of a seller's wholesale rates, and where a buyer is "not under any preexisting obligation under the terms of any interconnection agreement, power pool, or other highly integrated contractual or corporate arrangement" to make a purchase, FERC lacks jurisdiction to determine the buyer's prudence. Monongahela Power Company, et al. and Public Service Commission of the District of Columbia, FERC Docket Nos. ER87-330-000 and EL87-41-000, 39 F.E.R.C. para. 61,350, slip

op. at 10 (June 25, 1987). MP&L, looking forward from 1974, had no obligation to take any particular share of Grand Gulf; rather, the share that MP&L ultimately received would depend in part on its own actions. Under these circumstances, FERC has no authority to determine the prudence of MP&L's actions. Thus FERC's allocation to MP&L of 33% of Grand Gulf's costs cannot double as a finding that MP&L's customers are bound to pay those costs.

b. Mississippi is Free to Inquire Into MP&L's Pre-1982 Behavior

A state-level prudence inquiry makes sense only if MP&L had some freedom of action. The facts suggests that MP&L did have maneuvering room during the 1970's. For example:

Nothing in the 1973 System Agreement apparenty prevented MP&L from monitoring Grand Gulf's construction costs and acting to stop imprudent spending. Moreover, the

individual operating companies were free to propose off-system purchases. Indeed, the Commission has acknowledged "the need to recognize efforts of individual companies on the System and allow them to retain the benefits of units they own to the fullest extent possible." Middle South Energy, Inc. 32 F.E.R.C. (CCH) para. 61,425 at p. 61,961, aff'd sub nom., Mississippi Industries v. FERC, 808 F.2d 1525, rev'd in part on rehearing, 822 F.2d 1104 (D.C. Cir. 1987). [2]

Three of the four Middle South

---

[2] It is true that the Commission balanced this need with the need to provide an equitable sharing of nuclear investment costs. 32 F.E.R.C. at 61,961. But the purpose of this balancing was to arrive at a nondiscriminatory allocation of costs; not to block states from exercising their own statutory obligations to review the behavior of the companies they have authorized to do business in their states.

Of course, whether the operating subsidiaries had purchasing autonomy is a factual question that must be answered below. But it has not been answered.

subsidiaries have negotiated separate "Grand Gulf" settlements with their respective state commissions. In each such settlement, the subsidiary agreed, _inter alia_, to absorb a portion of the share of Grand Gulf allocated to it by the FERC decision. These settlements, which are summarized in the margin, suggest that the companies viewed themselves as vulnerable to state-level prudence challenges. [3] The

---

[3] _Arkansas Power & Light ("AP&L")_: The Arkansas Public Service Commission, by order dated September 9, 1985 in Docket Nos. 84-249-U and 85-198-U, approved a Stipulation and Settlement. Paragraph 4 of the Joint Motion for approval of the settlement states:

> Under the terms of the Stipulation and Settlement Agreement, AP&L will permanently retain a significant portion of the costs of power from Grand Gulf Unit 1 which has been allocated to AP&L by the FERC in its Opinion No. 234 dated June 13, 1985.

Paragraph 1(a) of the Stipulation and Settlement Agreement then states, in relevant part:

> Effective on September 1, 1985,

> AP&L will permanently retain the Arkansas retail allocation of the proportions of the costs associated with its allocated share of the power available to MSE from Grand Gulf Unit 1, as shown in Table 1 set forth below which proportions are stated in terms of percentages of MSE's share of Grand Gulf Unit 1 ("Retained Share")....The proportionate reductions in revenues from AP&L's Arkansas retail customers under this subparagraph will be permanent and will never be recovered from AP&L's Arkansas retail customers except as provided in paragraph 3 of this Agreement.

Paragraph 3 in turn permits AP&L to sell the capacity and energy available from its Retained share to certain third parties, or to AP&L's retail customers if AP&L is unable to sell to such third parties; AP&L is permitted to keep the proceeds of such sales without reducing the revenue requirement to be recovered from the retail customers.

<u>Louisiana Power & Light ("LP&L")</u>: The Louisiana Public Service Commission ("LPSC"), by order dated November 14, 1985 in Docket No. U-16945, approved certain emergency rate relief in return for LP&L's agreement to 6 conditions proposed by the LPSC staff. Condition 1 states:

> Middle South Energy, Inc. must agree to accept the permanently retained percentage (18%) of the

settlements have produced subsidiary-by-subsidiary rates that possibly vary with each subsidiary's bargaining power and risk aversion. In effect, the individual subsidiaries, through these agreements, have imposed underrecovery on the MSU system. This practice appears to contradict the MP&L's clain implicit claim that it lacks

---

LP&L share of Grand Gulf 1 under the terms outlined to the Commission, and offered by MSE, in July....A minimum net annual reduction in rates of $15.6 million would be guaranteed by MSE for 10 years. Alternatively, if MSE refuses to accept this proposal, LP&L would absorb the 18 per cent reduction on the same terms. This agreement would settle the Grand Gulf appeal.

<u>New Orleans Public Service Inc. ("NOPSI")</u>: In City Council Resolution R-86-112, issued on March 20, 1986 in Docket No. CD 85-1, the New Orleans City Council (the body which sets NOPSI's rates) offered NOPSI rate relief on certain conditions, including a promise that "[i]n total, NOPSI will permanently absorb $51.2 million of unrecovered Grand Gulf 1 costs." NOPSI accepted the offer.

purchasing autonomy.

FERC has made no finding whether MP&L's prudently exercised this autonomy. FERC's central concern in the Grand Gulf proceedings was cost allocation. As FERC stated: "The major issue in Docket No. ER82-616 [the Grand Gulf Agreement] is who among the four MSU operating companies should bear the costs of [Grand Gulf], and in what proportions." J.S. App. at 79a. Similarly, FERC stated that its decision concerned whether the rates "among those companies" are just and reasonable. J.S. App. at 101a. FERC did not purport to determine the prudence of MSU or any of its subsidiaries.

MP&L argues that because Sections 205, 206 and 306 of the Federal Power Act authorize state participation in FERC proceedings, state prudence review is superfluous (and preempted). This argument begs the question whether FERC may

preempted state prudence review. States seek to protect against discriminatory allocations of power plant investments, whether or not the investments are prudent. That interest alone explains the state participation provisions of Sections 205, 206 and 306.

3. FERC Did Not Preclude State Review of MP&L's Current and Future Efforts to Ease Its FERC-Imposed Burden

Grand Gulf has created excess capacity on MP&L's system. MP&L now has a duty now to minimize the cost of this capacity to its customers. It may be that the 1982 System Agreement, as interpreted and modified by FERC, imposes this capacity on MP&L. It also may be that the MPSC may not shield MP&L from this capacity. But nothing prevents the MPSC from questioning whether MP&L is managing its excess capacity prudently.

Therefore, MPSC must be free to

question the prudence of MP&L's effort, or lack of effort, to resell its excess capacity to others. FERC has held that "the Federal Power Act does not confer jurisdiction upon this Commission to dictate to a potential wholesale purchaser of power the particular supplier who it must purchase from." Monongahela Power Co., et al., supra, slip op. at 16. At least where the purchaser has purchasing freedom, FERC may not interfere with how that freedom should be exercised. Nor may the Commission dictate, once a buyer has made its purchase, how that buyer should minimize its net purchase costs. Even an affiliated buyer lacking purchasing freedom may have freedom to resell its excess. How well it does so is a matter for state review.

In Appeal of Sinclair Machine Products, Inc., 498 A.2d 696 (N.H. 1985), the Court held that FERC's approval of a wholesale

rate did not relieve the state commission of its obligation to inquire into the buying utility's "continued participation" under that rate. 498 A.2d at 705. While MP&L, unlike the buying utility in Sinclair, may not be free to opt out of Grand Gulf costs on one year's notice, 498 A.2d at 704, MP&L may achieve the same result by reselling its Grand Gulf-created excess off-system. The prudence of its attempts to do so must be evaluated by the state commission.

This Court's holding in Nantahala confirms the state's latitude over this matter. The Court there described as "perfectly sensible" the possibility of a "divergence between wholesale and retail rates ... if costs other than those resulting from the purchases of FERC-regulated power or gas were to decrease." 106 S.Ct. at 2357 (emphasis in original) (citing Narragansett Electric

Company v. Burke, 119 R.I. 559, 381 A.2d 1358, 1363 (1977), cert. denied, 435 U.S. 972 (1978); Public Service Co. of Colorado v. Public Utilities Commission, 644 P.2d 933, 941 (Colo. 1982)). If retail rate divergence from wholesale rates is permissible on grounds that the FERC-approved price increase was offset by savings experienced in other areas, Narragansett, supra, 381 A.2d at 1363, then divergence must be permitted where savings should have been experienced in other areas. [4]

---

[4] If the MPSC did disapprove a portion of MP&L's FERC-allocated share of Grand Gulf costs on grounds that MP&L imprudently failed to sell its excess off-system, the result would be quite similar to that envisioned in the Arkansas Power & Light ("AP&L") settlement approved by the Arkansas Public Service Commission, described in Part I.A.2.b, supra. In that settlement, AP&L agreed to absorb a certain portion of its FERC-allocated share of Grand Gulf, rather than recover the full costs of that share from its retail customers. If AP&L is able to sell this excess portion to third-parties, it may retain the revenues and thus reduce the

B. Nantahala, Which Assumed the Unavailability of Off-System Sources, Does not Preclude State Prudence Review Based on the Availability of Off-System Sources

MP&L and others argue that Nantahala rules this case. But Nantahala assumed that on-system power only was available to the buying utility. As this Court stated: "No source of power besides entitlement and purchased power from TVA is said to be available to Nantahala." 106 S.Ct. at 2360. In the decision that Nantahala found to be preemptive, FERC had treated the affiliates as having access only to high-cost and low-cost TVA power, and ordered an allocation of that power between two affiliated entities. The North Carolina Utilities Commission similarly assumed only TVA power was available, but ordered a different allocation.

Nantahala thus raised no issue as to

---

amount it is required to absorb.

whether the buying utility could have reduced its dependence on high-cost TVA power by purchasing from off-system sources. Nantahala never decided the issue in this case: whether MP&L's failure to seek off-system sources was imprudent.

FERC [illegible] Nantahala-based attack misperceives the issue. FERC argues that it rejected the alternative of MP&L's purchasing less Grand Gulf power and relying instead on lower cost sources, such as the system power pool. See J.S. App. at 124a n.19. But FERC never inquired whether MP&L was free to purchase off-system sources instead of commiting to Grand Gulf, or what off-system sources were available; nor did FERC ever inquire into whether MP&L could have reduced its contribution to system demand through conservation-oriented load management. That the FERC allocation now places "limitations ... upon [MP&L's] available sources of low-cost power,"

Nantahala, 106 S.Ct. at 2358, does not mean that MP&L labored under such limitations in the 1970's. [5]

In Part I.A.2.a, supra, we argued that by careful load management in the 1970s, MP&L could have reduced its contribution to system demand and thereby reduced its responsibility for Grand Gulf. Put another way, MP&L could have sought a non-system power source -- conservation. With this option available, Nantahala, with its assumption of no non-system power sources, should not apply.

In the context of the instant case, "trapped costs" evidence not jurisdictional

---

[5] For similar reasons, the holding in Appalachian Power Co. v. Public Service Commission of West Virginia, 812 F.2d 898 (4th Cir. 1987) does not apply to this case. The Court there found that "there is no alternative source of power for APC to choose other than that available through the AEP system, and the only access to that power is over the EHV lines whose costs are allocated by the [system agreement for sharing transmission costs]." 812 F.2d at 903.

conflict, but contractual and regulatory risk. The FERC-imposed purchase obligation is analogous to any contractual restriction. Similarly, Mississippi's denial of MP&L's request to recover its Grand Gulf responsibility will not result in other states bearing more, as FERC has suggested. A MPSC prudence denial would force MSU shareholders, not other MSU subsidiaries, to bear the unrecovered cost. Indeed, that is the purpose of the FERC allocation. By establishing each subsidiary's percentage responsibility, the FERC decision protects each subsidiary's customers from the burdens incurred by the other subsidiaries.

C. Sections 205 and 206 of the Federal Power Act Do Not Authorize Solutions to Regional Power Planning Problems

MP&L appears to assert that the FERC allocation is preemptive because it reflects FERC's judgment that the regional

interest overrides any differing state view of its own welfare. MP&L Br. at 33-34. MP&L cites no such judgment by FERC.

That is not surprising, because FERC had no power in this proceeding to dictate a regional power planning solution. Only in a special proceeding called for under 16 U.S.C. sec. 824a-1 may FERC exempt utilities from state laws or regulations, and then only where such exemption is necessary to ensure "economic utilization of facilities and resources in any area." Moreover, such exemption would not be permissible where the state rule is "designed to protect public health, safety or welfare, or the environment or conserve energy...." The instant case was conducted under Sections 205 and 206 of the Federal Power Act, not under the specialized proceeding envisioned in 16 U.S.C. sec. 824a-1.

That provision demonstrates that

Congress foresaw certain special circumstances where regional power supply needs could override particular state interests. But Congress' need to enact a special provision to deal with this potential situation confirms that Sections 205 and 206 do not authorize such action.

In any event, MP&L's argument -- that FERC's decision must be preemptive because it reflected a judgment that regional needs superseded in-state needs -- goes too far. The same rationale could be applied to FERC-approved contracts between unaffiliated companies. As discussed in Part III, infra, preemption certainly cannot apply in that context. Furthermore, MP&L's argument is not consistent with the facts. FERC found that the planning on the Middle South system was geared toward "the best interests of the System as a whole," J.S. App. at 113a, not for the region as a whole.

II. THE FEDERAL POWER ACT DOES NOT SHIELD A UTILITY FROM COMMITMENTS MADE TO STATE REGULATORS

A. MP&L and MSE Accepted the MPSC-Imposed Risk of Grand Gulf Underrecovery

In 1974, MP&L and MSU approached the MPSC, seeking permission to construct Grand Gulf. See "Joint Petition" (April 12, 1974), App. to Motion to Dismiss at 1-20. The MPSC granted the Joint Petition, with two conditions. See "Order Granting Certificate of Public Convenience and Necessity" (May 29, 1974), App. to Motion to Dismiss at 21-40. By accepting these conditions, MP&L and MSU undertook the risk that they might be unable to recover all of Grand Gulf's costs.

As to the first condition, the Certificate of Convenience and Necessity ("CCN") incorporated MP&L's representation that its participation in Grand Gulf was necessary so that "[MP&L] may render adequate and dependable service to its

customers and service areas...." App. to Motion to Dismiss at 14 (MP&L and MSE proposal), 37 (MPSC finding). Implicit in MP&L's statement and the MPSC's adoption thereof is a condition: that if during the construction period it developed that Grand Gulf will not be necessary for MP&L to "render adequate and dependable service to its customers and service areas," MP&L would act to minimize its participation in the plant. MP&L did not propose, and MPSC did not agree, that if continuation of the plant was necessary to meet MSU system needs but not MP&L's needs, Mississippi customers would remain exposed to the plant's costs.

Second, the Commission conditioned its approval on a promise that MP&L's customers would be protected from a certain portion of the risk of excess capacity. This protection took the form of MPSC's insistence that MP&L's customers would be

treated as if MSE was a party tothe System Agreement. Specifically, the CCN states that "[a]t an appropriate time, the System Agreement will be amended to make MSEI a party thereto." Appendix to Motion to Dismiss at 33. The significance of this condition was explained by the Mississippi Supreme Court (J.S. App. at 5a-6a):

> We cannot stress enough the implications of this agreement embodied in the 1974 Order [i.e., the agreement among the MPSC, MP&L and MSEI that the 1973 System Agreement would be amended to include MSEI as a party]. MSEI is not an operating company; therefore, it does not require any generating capacity for itself. Under the 1973 Agreement, it would always be a long company, with excess capacity to allocate among the short companies. Grand Gulf, its most recently installed generating unit, would become MSEI's participation unit, from which the costs to the short companies would be calculated. ... MP&L remains a long company. Under the 1973 Agreement, it would not be required to share in the allocation of costs of Grand Gulf unless and until it required additional capacity to meet its needs. Even if ... MP&L had become a short company, it would have had to pay

> costs associated with Grand Gulf only to the extent that it required additional capacity. [6]

In short, making MSEI a party to any system sharing agreement would shift a major risk -- that Grand Gulf would create system excess capacity -- away from long companies.

MP&L's argument that because FERC made no finding of conditioning, no conditioning took place, is untenable. FERC has no authority to determine what if any conditions MPSC imposed. Whether the CCN imposed a condition on MP&L is a matter of interpretation for Mississippi courts. The Mississippi Supreme Court has made its

---

[6] See also Mississippi Industries v. FERC, 808 F.2d 1525, 1533 ("[a]t first it was contemplated that MSE would become a party to the System Agreement. Under this plan all of Grand Gulf would be a 'participation unit' and responsibility for the plant's capacity would shift among the operating companies to the degree they were short"), rev'd in part on rehearing, 822 F.2d 1104 (D.C. Cir. 1987); J.S. App. at 86a.

finding. Even if FERC does have authority to issue an authoritative interpretation of a state-issued CCN, its purported finding is still subject to appeal.

B. If States May Bar a Utility Affiliation Outright, They Certainly May Condition that Affiliation on Utility Acceptance of Risk

States are free to bar utilities under their jurisdiction from affiliating with other utilities. See Baltimore Gas and Electric Co. v. Heintz, 760 F.2d 1408 (4th Cir. 1985). It necessarily follows that states must be permitted to condition affiliations, and the actions of affiliates, on their agreement to bear certain risks.

Absent the state's right to impose such conditions, traditional state influence over plant construction decisions could vanish with a shuffling of corporate papers. For example, supppose Company X seeks permission from its state regulatory

commission to participate in Company Y's plan to build a coal plant in another state. The first state refuses permission, on grounds that cheaper alternatives exist. In response, Company X becomes a subsidiary of Company Y, and the two companies execute a contract and obtain FERC approval. Company X now would assert that its state commission was preempted from disapproving the purchase.

State governance of the "need for new power facilities, their economic feasibility, and rates and services" is ingrained in our nation's policymaking infrastructure. See Pacific Gas & Electric Co. v. State Energy Resources Conservation and Development Comm'n, 461 U.S. 190, 205-07 (1983). These "'historic police powers ... were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'" Id., 461 U.S. at 206 (quoting Rice v. Santa Fe

Elevator Corp., 331 U.S. 218, 230 (1947)). Congress had no intention, manifest or otherwise, to permit use of the holding company structure to avoid commitments made to garner state support for major utility investments like Grand Gulf.

Thus FERC's argument that any MPSC conditioning was invalid because it tied FERC's hands [7] is premised on a misinterpretation of the CCN. The conditions do not bind FERC; they bind the utility. MSU, by agreeing to limit the share of Grand Gulf costs it would impose on Mississippi (such limit to be effected indirectly by making MSE a party to the System Agreement), took the risk that it might not be able to impose the remaining shares on the other states. FERC's allocation decision has precluded MSU from

---

[7] J.S. App. at 103a; see also Mississippi Industries, supra, 808 F.2d at 1549-50.

shifting Mississippi costs to the other states. But the MPSC-imposed condition remains in force. MSU and MP&L now must absorb the risk they undertook. [8]

C. The Drafters of the Federal Power Act Did Not Intend The Holding Company Form to Become a Tool for Dismantling State Regulatory Structures

---

[8] For a company serving multiple jurisdictions to bear the risk of inconsistent decisions is hardly new. As FERC has held:

> [I]f PEPCO were to sell the Ohio Edison system power both at wholesale and directly at retail, any future Commission decision of whether PEPCO prudently purchased the Ohio Edison system power, for the purpose of determining the lawfulness of PEPCO's rates for sale of that power at wholesale, would not as a general matter bind a State commission in setting rates for PEPCO's sale of the power at retail.

Monogahela Power Co., et al., supra, slip op. at 11. Cf. Moorman Manufacturing Co. v. Bair, 437 U.S. 267, 278 (1978) (Commerce Clause not violated by the "risk of duplicative taxation [which] exists whenever the States in which a corporation does business do not follow identical rules for the division of income").

Absent MSU's holding company status, its obligation to adhere to the MPSC condition, or bear the resulting penalties, would be unquestioned. If there were a single corporation doing business across several states, there would be no wholesale transaction and no FERC regulation. Instead, each state would determine, independent of the other states, its allocable share of total costs, and set rates accordingly. Such allocation of costs incurred on a multijurisdictional utility system are commonplace in utility regulation. [9]

---

[9] See, e.g., Washington Utilities and Transportation Commission v. Pacific Power & Light Company, 68 P.U.R.4th 396, 417-18 (Washington Utilities and Transportation Commission 1985). The Washington Commission there stated that, in assigning responsibility among jurisdictions for costs of utility operations,

> [e]ach of the regulating jurisdictions must act in a reasonable manner, pursuant to its own statutes and to state and federal constitutional law. Each

MSU is not a single corporation. In its hands, the holding company structure, in conjunction with the Federal Power Act, becomes a tool for dismantling commitments made by local utility managers to state regulators. But Congress long ago decided that state regulation should be immune from manipulation of corporate form. See North American Co. v. SEC, 327 U.S. 686, 704 (1947) (one goal of the Public Utility Holding Company Act of 1935, 15 U.S.C. sec. 79 et seq., was "to rejuvenate local utility management and to restore effective state regulation, both of which had been

---

> state need not subscribe to any aspect of rate making just because one or more other jurisdictions do so....The definition of rate base may differ widely among jurisdictions, so that one state's regulatory rate base might be substantially larger or smaller than the figure calculated upon another state's methodology.

See also Washington Water Power Company, 65 P.U.R.4th 100, 103-105 (Idaho Public Utilities Commission 1985).

seriously impaired by the existence and practices of nation-wide holding company systems").

The Federal Power Act was enacted simultaneously with the Public Utility Holding Company Act as part of the Public Utility Act of 1935. That Act "had two primary and related purposes: to curb abusive practices of public utility companies by bringing them under effective control, and to provide effective federal regulation of the expanding business of transmitting and selling electric power in interstate commerce." Gulf States Utilities Co. v. FPC, 411 U.S. 747, 758 (1973). MP&L's effort to find in the Federal Power Act authority to use its affiliation with other utilities to escape its state-level commitments would place these harmonious purposes in direct conflict.

III. FERC PREEMPTION SHOULD NOT APPLY WHERE THE BUYING UTILITY HAS FINANCIAL INDEPENDENCE FROM THE SELLING UTILITY

MP&L asserts that "any state's jurisdiction to investigate the 'prudency' of costs incurred under FERC rate schedules is preempted by the FPA. Under the filed rate doctrine, all such expenses must be treated as "a reasonably incurred operating expense." MP&L Brief at 26. MP&L's attempt to preempt state review of a utility-buyer's arrangements with unaffiliated entities strays far from the reasoning of Nantahala.

The basis for asserting preemption in the affiliated entity context is the filed rate doctrine. The doctrine entitles the seller to receive the rate filed at FERC. The reasoning appears to be that state denial of the buyer's recovery, where the buyer is the corporate alter ego of the seller, effectively denies the seller his FERC-filed rate. This argument has no

application to the unaffiliated buyer. Corporate independence is financial independence. The requirements of filed rate doctrine are fulfilled when the seller receives his FERC-filed rate. What happens to the buyer at the hands of duly enacted state standards is of no legitimate concern to FERC.

CONCLUSION

For the foregoing reasons, _amici_ Consumer Federation of America, Environmental Action and Citizen/Labor Energy Coalition respectfully request this Court to affirm the decision of the Supreme Court of Mississippi.

Respectfully submitted,

Scott Hempling
Counsel of Record

Environmental Action
Foundation
1525 New Hampshire Ave.
Washington, DC 20036
(202) 745-4871

Of counsel:
Roger Colton
72 Maple St.
Belmont, MA 02178

January 22, 1988

CERTIFICATE OF SERVICE

I hereby certify that on January 22, 1988, I served a copy of the foregoing document on those persons listed below, by depositing a copy thereof in the United States mail, postage prepaid, or by equivalent method of service.

Rex E. Lee
1722 Eye St.
Washington, DC 20006

John L. Maxey II
304 N. Congress St.
P.O. Box 22666
Jackson, MS 39205

Jesse C. Pennington
P.O. Box 22887
Jackson, MS 39205

Scott Hempling

AMICUS CURIAE

BRIEF

(14)

No. 86-1970

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,

Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN, Attorney General, and THE MISSISSIPPI LEGAL SERVICES COALITION,

Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF FOR THE NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER ADVOCATES AS AMICUS CURIAE

STEVEN W. HAMM*
Consumer Advocate of South Carolina and Chairman of NASUCA's Electric Committee

National Association of State Utility Consumer Advocates
2801 Devine Street
Post Office Box 5757
Columbia, SC 29250
(803) 734-9464

*Counsel of Record

RAYMON E. LARK, JR.
Ass't Consumer Advocate of South Carolina and Member of NASUCA's Electric Committee

ELIZABETH ELLIOT
Ass't Staff Counsel for Nevada Attorney General's Office of Advocate for Customers of Public Utilities, NASUCA Members

TABLE OF CONTENTS

TABLE OF AUTHORITIES

No. 86-1970

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN, Attorney General, and THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

BRIEF FOR THE NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER ADVOCATES AS AMICUS CURIAE

INTEREST OF AMICUS CURIAE

The National Association of State Utility Consumer Advocates (NASUCA) files this brief as *amicus curiae* urging the Court to affirm the decision below of the Supreme Court of Mississippi. NASUCA members represent retail electric consumers in thirty-four states

and the District of Columbia. NASUCA urges this Court to refrain from reversing the decision below. A reversal will have a dramatic, immediate, and negative impact on the traditional scope of state regulation of investor-owned public utilities. Those participating as consumers and advocates for consumers in a changed state regulatory process will be detrimentally affected as well. NASUCA submits this brief with the consent of the parties, and files written verification of such with the Clerk pursuant to Supreme Court Rule 36.2.

Any investor-owned electric utility holding a state certificate granting it the privilege to serve (without threat of competition), the state's retail customers is in turn obligated to submit itself to a long-standing tradition of state regulation. To effectuate its service to retail customers, the investor-owned utility may either generate its own power, or purchase energy from generating sources beyond its state's borders. The utility may also choose to market any of its own excess energy to out-of-state distributing utilities. The investor-owned utility's ability to participate in this wholesale,

interstate market is a function of its own unique transmission and generating constraints.

An investor-owned utility's non-retail, wholesale activities impact retail rates and the utility's captive ratepayers. Therefore, the state regulatory authority charged with overseeing the activities of investor-owned public utilities is interested in the costs at which the utility purchases and sells energy in the wholesale market. For instance, the state regulator may have to decide whether retail customers should pay for high-priced energy purchased on the wholesale market, when other less expensive energy was available. In this example, the state regulator does not decide whether the wholesale transaction should be allowed, or at what price that wholesale purchase should be made. Those determinations are admittedly left for federal regulators. Rather, the state regulator asks only whether and to what extent retail customers should be forced to pay for a bad wholesale deal-- an imprudent decision by the utility. NASUCA members actively pursue these issues before their State regulatory commissions.

Wholesale, interstate rate settings are governed by the Federal Power Act and administered by the Federal Energy Regulatory Commission (FERC). However, the prudence of an investor-owned utility's decision to enter into wholesale transactions and the impact of such decisions on a utility's retail customers are *not* subject to review under the Federal Power Act, and thus are not within the scope of authority of FERC. Rather, the authority to both determine the prudence of an investor-owned utility's decision to conduct wholesale transactions, and to decide how to treat the impact on retail customers of a utility's decision to enter into wholesale transactions have been expressly reserved for the States.

In the proceeding at bar, the Supreme Court of Mississippi recognized the legislative duty of the Mississippi Public Service Commission (MPSC), to review the prudence of Mississippi Power & Light Company's (MP&L) decision to enter into a wholesale purchase of energy from Grand Gulf Generating Unit One. The Mississippi high court found that when

reviewing the impact of MP&L's decision to enter into this wholesale purchase on the State's retail customers, the MPSC had ignored its statutory obligation to determine the prudence of MP&L's wholesale, interstate activities.[1] The Mississippi Supreme Court thus remanded the action to the MPSC for further consideration of the prudence-related issues. NASUCA is deeply concerned that reversal of the Supreme Court of Mississippi's Order will improperly call into question the very foundation of traditional utility regulation-- the responsibility of the States to determine whether retail rates are just and reasonable.

NASUCA is a national organization comprised of thirty-seven members in thirty-four states and the District of Columbia. Members of NASUCA represent the interests of electric and natural gas retail consumers in proceedings involving investor-owned public utilities before their individual State regulatory commissions, FERC, and State and Federal courts. Resolution of

[1]The MPSC had specifically reserved the issue of prudence for later consideration but then failed to conduct the necessary analysis. J.S.App. 9a

issues raised in this proceeding will affect the very nature of traditional utility regulation and thus is of great importance to consumers of investor-owned utilities and to every NASUCA member.

ARGUMENT

I. THE FEDERAL POWER ACT ON ITS FACE RESERVES FOR THE STATES THE AUTHORITY TO CONDUCT PRUDENCY REVIEWS OF GENERATING UNITS AND POWER PURCHASES WHEN SETTING RETAIL RATES.

A decision on the merits[2] of the case at bar should affirm the Order below of the Mississippi Supreme Court. Subchapter II of the Federal Power Act, 16 U.S.C. §§ 824-824k, prescribes the extent to which FERC may regulate electric utilities engaged in the transmission or sale of energy in interstate commerce. Congress expressly stated its intent to narrow FERC's authority in this area when it limited FERC's regulatory power to

[2] *Amicus* NASUCA addresses only the substantive questions before the Court in this Brief, and is silent as to the issues raised in the pending Motion to Dismiss for Lack of Jurisdiction. This silence should not be construed as opposition to that pending Motion, however.

"only to those matters which are not subject to regulation by the States." 16 U.S.C. §824 (a).

In deciding questions regarding the boundaries of FERC's authority to regulate under Subchapter II of the Federal Power Act, the United States Supreme Court has maintained the distinction between wholesale, interstate transactions (for which FERC has exclusive jurisdiction), and retail, intrastate service (the regulation of which has been left wholly to the States).

> The line of the statute was ... clear and complete. It cut sharply and cleanly between sales for resale and direct sales for consumptive uses.

Panhandle Eastern Pipe Line Company v. Public Service Commission of Indiana, 332 U.S. 517, (1947).[3] *See, also, United States v. Public Utilities Commission of California*, 345 U.S. 295 (1953).

Congress never intended that FERC's exclusive authority to regulate in the wholesale marketplace should curtail the States' exclusive authority to regulate

[3] *Panhandle* was decided under the Natural Gas Act rather than the Federal Power Act. This Court has determined that the relevant provisions of the two statutes are parallel, however, and has cited to cases interpreting these provisions interchangeably. *Arkansas Louisiana Gas Company v. Hall*, 453 U.S. 571, 577, n. 7 (1981).

the retail operations and rates charged by certificated investor-owned public utilities. In *Connecticut Light and Power Company v. FERC*, 324 U.S. 515, 525 (1945), the Court reviewed the legislative history of the Federal Power Act and determined that Congress intended a "constant purpose to protect rather than to supervise authority of the states." This principle was further elaborated in *Panhandle, supra*, where the Court stated:

> The Act, though extending federal regulation, had no purpose or effect to cut down state power. On the contrary, perhaps its primary purpose was to aid in making state regulation effective.

Panhandle, 332 U.S., at 517.

Put simply, FERC's exercise of authority under 16 U.S.C §824-824k does not diminish the States' authority to regulate the conduct and operations of certificated investor-owned utilities charged with serving captive, retail markets. The States are free to determine whether a retail utility is conducting its operations in a prudent manner, and whether expenditures have been prudently incurred. Furthermore, the States are free to determine how the effects of a public utility's imprudent conduct should impact its captive, retail customers.

A. FERC HAS RECOGNIZED THE STATES' AUTHORITY TO DETERMINE PRUDENCE OF WHOLESALE TRANSACTIONS WHEN DECIDING THEIR IMPACT ON RETAIL CONSUMERS.

FERC itself has recognized the authority of the States to determine the prudence of a public utility's decision to enter into a wholesale transaction. When approving wholesale rates under an interstate purchase contract, FERC has repeatedly refused to consider the issue of prudency and referred the parties requesting such review to the state regulatory commissions. FERC decides whether the terms of a wholesale transaction are appropriate, while the States determine whether and to what extent the transaction should impact retail rates.

In *Pennsylvania Power and Light Company,* 23 FERC ¶ 61,325 (1983), FERC was asked to determine whether a particular purchase for which it was setting a wholesale rate was prudent in light of the purchasing utility's need for supply and the alternatives available to it. FERC found that its authority to question the prudence of a wholesale transaction under the Federal Power Act was limited to whether "the rates, terms, and provisions under which PP&L is selling unit power ...

appear to be just and reasonable." *Pennsylvania Power & Light*, at 61,716. Issues of a purchaser's need for energy or the availability of less expensive alternatives were not "matters which the Commission must consider in determining whether this contract is just and reasonable and in the public interest under the Federal Power Act." *Pennsylvania Power & Light*, at 61,716. In refusing to consider these prudence issues as requested by the New Jersey Board of Public Utilities and the New Jersey Public Advocate, FERC ultimately found:

> We do not view our responsibilities under the Federal Power Act as including a determination that the purchaser has purchased wisely or has made the best deal available. However, these are legitimate concerns of the State commissions....

Pennsylvania Power & Light, at p. 61,716.

FERC came to a similar conclusion in *Southern Company Services, Inc.*, 26 FERC ¶61,360 (1984). Again FERC refused to consider an intervenor's suggestion that less expensive supply alternatives were available and that the buyer was acting imprudently by choosing to participate in the wholesale transaction:

> [T]he Commission is not empowered to disapprove or modify a power sales agreement on the grounds that the buyer may not be making the best possible deal. As we held in another case involving Southern Companies [20 FERC ¶ 61,332 (1982)], the question of the prudence of a utility's power purchases is properly an issue in the buying utility's [state] rate case where it seeks to pass the costs of its purchased power on to its [retail] ratepayers.

Southern Companies, 26 FERC ¶61,360, at 61,795 (footnotes omitted). *See also,Southern Company Services, Inc.*, 28 FERC ¶ 61,349 (1984).

FERC has clearly expressed its determination to stay away from comprehensive review of the prudence of a retail public utility's decision to enter into a wholesale transaction. The FERC has relied on the same analyses set out above in leaving prudence issues to the States (*supra*, at 6-9).[4]

The issue before the Court in the case at bar is identical to that decided by FERC in the cases cited above--*whether state regulators have the authority to*

---

[4] The FERC cases cited here were decided during the same period in which FERC was conducting hearings on and considering the allocation of Grand Gulf. *See*, initial decisions in *Middle South Energy, Inc.*, 26 FERC ¶63,044 (1984) and *Middle South Energy, Inc.*, 30 FERC ¶ 63,030 (1985) ; final decisions in *Middle South Energy, Inc.*, 31 FERC ¶ 61, 305 (1985) and *Middle South Energy, Inc.*, 32 FERC ¶61,425 (1985). As pointed out later (*see, infra*), at 19-20, FERC did not undertake any detailed after-the-fact prudence review of Grand Gulf costs.

determine the prudence of a certificated, investor - owned public utility's decision to enter into wholesale transactions. Then, as now, the question must be answered in the affirmative. The Federal Power Act does not affect the States' authority to determine whether retail rates are just and reasonable. The States are thus free to ask whether a public utility's decision to participate in a wholesale transaction was prudent before placing the costs of that wholesale purchase into retail rates.

B. OTHER COURTS HAVE RECOGNIZED THE AUTHORITY OF STATE REGULATORS TO DETERMINE THE PRUDENCE OF WHOLESALE TRANSACTIONS WHEN DECIDING THEIR IMPACT ON RETAIL CONSUMERS.

The Mississippi Supreme Court is not the first to grapple with the issue at hand. In *Commonwealth Electric Company v. Department of Public Utilities*, 397 Mass. 361, 491 N.E.2d 1035 (1986), the Massachusetts Supreme Judicial Court was asked to decide whether the State regulatory agency had the authority to question the prudence of the public utility's wholesale

power purchase. The purchase was necessary to replace native generation lost during an unscheduled, catastrophic shut-down of one of its own nuclear units. After reviewing the Federal Power Act and its implementing regulations, the Massachusetts Court determined that "while the DPU cannot inquire into the reasonableness of wholesale rates fixed by FERC ... the DPU may inquire whether a purchaser ... is warranted in agreeing to purchase at such a rate considering the alternatives." (citations omitted) *Commonwealth Electric*, at ___, 1045.

In addition, the Commonwealth Court of Pennsylvania was asked to decide whether the state utility commission could disallow purchased power expenses incurred pursuant to a FERC-approved contract and rate. *Pike County Light and Power Co, v. Pennsylvania Public Utility Commission*, 77 Pa.Commn. 268, 456 A.2d 735 (1983). The Pennsylvania Commission had determined that, given the availability of less expensive alternative sources of supply, the utility

had imprudently elected to purchase more expensive energy from its parent. The Pennsylvania Court looked at the Federal Power Act and FERC regulations and found that, in approving a wholesale contract and rate, FERC is not required to analyze the purchaser's financial capabilities or its alternatives. FERC asks only "whether it is just and reasonable for *that* [selling] *company to charge* a particular rate, but makes no determination of whether it is just and reasonable *for Pike to incur* such a rate as an expense." *Pike County,* at ___, 738 (emphases in original).[5] The Court went on to hold:

> So while the FERC determines whether it is against the public interest for Orange & Rockland [the seller] to charge a particular rate in light of its costs, the PUC determines whether it is against the public interest for Pike [the purchaser] to pay a particular price in light of its alternatives. The regulatory functions of the FERC and PUC thus do not overlap....

Pike County, at ___, 738. *See also, Appeal of Sinclair Machine Products, Inc.*, ("the PUC may always inquire

---

5 This point is wholly consistent with FERC findings referred to in Argument I.A. above.

into the reasonableness of a utility's purchasing power under a FERC-approved rate given other purchase options available to the utility") 498 A.2d 696, 696 (N.H. 1985) and, *Kentucky West Virginia Gas Company v. Pennsylvania Public Utility Commission.*, ("the PUC has focused on an intrastate retailer and its options from among several pipeline suppliers to satisfy the retailer's duty to Pennsylvania customers. This scheme is within the category of regulatory questions reserved for the states") 650 F.Supp. 659, 667 (M.D. Pa. 1986).

In the case at bar, FERC has relied on its exclusive authority to regulate wholesale transactions in allocating shares of the output of Grand Gulf Unit One among four of Middle South Utilities' wholesale customers: its operating subsidiaries MP&L, Arkansas Power & Light Co. (AP&L), Louisiana Power & Light Co. (LP&L), and the New Orleans Public Service, Inc. (NOPSI). If it is assumed that FERC had authority to determine the Grand Gulf allocation,[6] that authority should not be

---

6 An issue not conceded, and not addressed in this Brief.

interpreted as limiting the authority of the States to determine the prudence of a retail utility's participation in a wholesale transactions-- especially when, as in the instant case, less expensive alternatives are available. J.S.App. 15a-16a. Neither can FERC's authority to set rates for wholesale transactions trample the States' authority to determine how the effects of a public utility's imprudent participation in wholesale transactions should impact the retail customers of that utility.

The observations of this Court in *Nantahala Power and Light Company v. Thornburg*, No. 85-568, ___ U.S. ___, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986), support this conclusion:

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price.*

Nantahala, ___ U.S. at ___, 106 S.Ct. at 2360, 90 L.Ed.2d at 958 (emphasis in original).

The Mississippi Supreme Court ordered the State's regulatory commission to rehear MP&L's request to

raise its retail rates, this time taking into account the question of MP&L's prudence in participating in wholesale transactions with Middle South Utilities and its fellow operating subsidiaries. In so doing, the Supreme Court of Mississippi was merely requiring the State regulator to fulfill its legislative duty to make a finding as to the justness and reasonableness of MP&L's proposed retail rates. *See,* Miss.Code Ann. §77-3-39 (1972). The authority of the MPSC to determine the prudence of MP&L's conduct, even conduct related to wholesale transactions, is not affected by FERC's authority to establish wholesale rates. Furthermore, should the MPSC's investigation into MP&L's wholesale dealings reveal imprudence on the part of MP&L and/or its management, the MPSC would then have the authority to determine how that imprudence should impact retail rates, and that excessive costs would not be trapped in retail rates. *Cf. Nantahala, supra,* at ___ U.S. at ___, 106 S.Ct. at 2359, 90 L.Ed.2d at 957 (legitimate wholesale rates not

included in retail rates are trapped; trapping is prohibited).

II. THE FEDERAL POWER ACT DOES NOT BAR STATES FROM DETERMINING PRUDENCE OF CONSTRUCTING GENERATING UNIT WHEN DECIDING IMPACT ON RETAIL CONSUMERS.

With one narrow exception allowing concurrent jurisdiction, the Federal Power Act reserves jurisdiction over generating units to the States. *See,* 16 U.S.C. §824e. That exception does not apply here.

The Mississippi Supreme Court held below that the "state regulatory body, in this case, the Mississippi Public Service Commission, must review the prudency of an investment such as Grand Gulf before it can enact rates based on its cost." J.S. App. 19a. The Mississippi Court framed the prudency question as "whether MP&L, MSEI and MSU acted reasonably when they constructed Grand Gulf 1, in light of the change in demand for electric power in this state and the sudden escalation of costs." J.S. App. 19a-20a. MP&L argues that the Federal Power Act preempts this type of review. *See,* Appellant's Brief, at 22. MP&L is wrong. The

Federal Power Act broadly prohibits FERC jurisdiction over generating facilities. The FERC:

> *shall not have jurisdiction*, except as specifically provided in this subchapter and subchapter III of this chapter, *over facilities used for the generation of electric energy....*

16 U.S.C. 824 (b)(1), (emphases added).

Thus the Federal Power Act reserves jurisdiction over generating facilities exclusively for the States. There is but one exception to exclusive State jurisdiction, which permits after-the-fact inquiries by FERC relevant to wholesale power rate settings. The Federal Power Act at 16 U.S.C. §824e (b) provides that on a special motion and "whenever it can do so without prejudice to the efficient and proper conduct of its affairs", FERC may conduct an after-the-fact review of costs associated with facilities "under the jurisdiction of the Commission:" *ie.* facilities related to interstate transmission or wholesale transactions. Thus, FERC may review, under this constrained procedure, the prudence of certain costs-- including the costs of constructing a generating unit-- when it establishes a wholesale rate. However, this process was not invoked

in the case of Grand Gulf, and the prudence of M.S.U. and MP&L's decisions to continue construction of the unit was never considered by FERC.[7]

Unlike transmission facilities or interstate energy sales, generating units are not subject to the Federal Power Act's designation of serving either wholesale or retail consumers. Generating units do not carry "wholesale" or "retail" designations because Congress has expressly denied FERC any jurisdiction over generating units. As discussed in detail above, FERC's authority is limited only "to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. §824 (b)(1). Thus, FERC can determine the rate at

[7] Two important caveats regarding FERC's authority under §824e must be noted. First, FERC is limited to an after-the-fact review of the prudency of construction costs. It is without authority or procedures to make a pre-construction determination of the need for new generation or the appropriateness of a particular construction proposal to a given situation (*e.g.*, coal vs. nuclear, baseload vs. peaking, 250 megawatts vs. 1000 megawatts). These determinations are reserved for the regulatory tradition, structure, resources, and expertise of the States. *See*, *infra*, at 21-23. Second, like other of FERC's specific ratemaking findings (*e.g.*, the appropriateness of including Construction Work in Progress in rate base or setting an allowable rate of return), prudency determinations made in wholesale rate settings would not be dispositive of prudency issues raised in State retail rate cases.

which the output from a generating unit can be transferred in the wholesale marketplace, but it is without jurisdiction over the generating unit itself. That authority has been left to the States.

Examples abound of Congress' mandate to leave jurisdiction over generating units to the States. The States, not FERC, are charged with making pre-construction determinations as to the need for a proposed generating unit. The States, not FERC, are charged with determining whether a proposed generating unit is appropriately conceived, sized, designed, and located to meet the utility's projected need. In Mississippi this authority is established under and governed by the Certificate of Need process. J.S. App. 5a.[8]

MP&L submitted itself to the jurisdiction of the MPSC in 1974 when it sought permission from the MPSC to begin constructing Grand Gulf Unit One. J.S. App. 5a. In making its finding, the MPSC determined that the

[8] Other State jurisdictions have developed more elaborate and comprehensive planning and pre-approval processes. *See*, discussion of the State "Least Cost Utility Planning Process," *infra*, at 23-25.

decision to construct a nuclear power plant of the size and configuration proposed was necessary and would not adversely effect MP&L's retail customers, given the best information available at the time. In the eleven years that elapsed between the granting of the Certificate of Need and the completion of Grand Gulf Unit One, it became painfully obvious that MP&L had made an expensive mistake. First, MP&L, and indeed the entire Middle South Utilities system, were glutted with so much excess capacity that Grand Gulf energy pushed MP&L's reserve margin to over 100%. J.S. App. 9a. Second, actual construction costs were more than twice projected costs (J.S. App. 13a), and oil and gas prices had decreased so that Grand Gulf energy was almost 200% more expensive than other available energy. J.S. App. 16a.

The output from Grand Gulf is shared under a FERC-approved contract and wholesale rate with LP&L, NOPSI, and AP&L. According to Appellants, that fact alone strips state regulators of their jurisdiction to review the prudence of the decision to continue the construction

of Grand Gulf Unit One or to determine how imprudence should affect *retail* ratepayers. Given the express language of Federal Power Act , however, this result is directly contrary to Congress' instructions that FERC "shall not have jurisdiction ... over facilities used for the generation of electric energy...." 16 U.S.C. § 824 (b)(1). It is, therefore, the responsibility of MPSC, and not FERC, to review the prudence of wholesale purchases whose cost are to be included in retail rates.

III. REVERSAL OF DECISION BELOW WOULD CAUSE ADDITIONAL BROAD, UNINTENDED, AND IMPROPER PREEMPTION OF STATE REGULATORY AUTHORITY.

A reversal of the Mississippi Supreme Court would disrupt, and possibly end, new cooperative intrastate efforts to avoid expensive mistakes in planning for and building power plants.

The discussions above have focused on the state regulator's obligation to protect retail electric consumers from the imprudent conduct of investor-owned public utilities. Most jurisdictions review imprudence in the context of retail rate cases-- after power plants are built

and billions of dollars spent. Some states, however, have begun supplementing this after-the-fact review with a comprehensive, up-front resource planning structure.[9] In so doing, these local jurisdictions are attempting to avoid the over-supply, over-cost situation which Grand Gulf has come to represent. Reversal of the decision at bar would derail this structure.

Under utility resource planning (commonly referred to as "Least Cost Utility Planning" or LCUP), all interested parties including the utility, state and local government, large industrial customers, commercial customers, and the residential consumer, may participate in utility planning decisions which the utilities formerly performed on their own. The utility is required to compare its resource plan proposal with *all* available resources including conservation, demand reduction, supply produced using alternative fuels or alternative generating techniques (cogeneration and small power production), and other traditional supply alternatives. Most importantly, LCUP requires a finding that of all the

---

[9] *See, e.g.*, Nev.Rev.Stat. 704.735-751.

potential resources available, the utility's chosen option will have the lowest dollar impact on its retail customers.

LCUP offers the utility a reduction in financial risk since all affected parties are joined in the planning effort. LCUP is enforced pursuant to the state regulator's authority to determine the prudence of a decision that might very well involve wholesale transactions. Without this enforcement mechanism, utility managers have little incentive to give up their historical control to determine and plan for the utility's future needs. The LCUP process is in great jeopardy if the Court reverses the Order of the Mississippi Supreme Court, thereby eliminating the States' regulation of utility prudence matters.

IV. THE COURT MAY PREFER TO REMAND THIS CASE SINCE THE MPSC HAS NOT YET ADDRESSED THE PRUDENCE OF MP&L'S PURCHASE OF ENERGY FROM GRAND GULF.

The question of whether energy purchased from Grand Gulf Unit One would necessarily be included in MP&L's retail rates has not yet been determined since

the MPSC has not conducted its prudency review. In *Nantahala, supra*, the Court assumed without deciding the issue that a state utility commission had the authority to exclude from retail rates the costs of wholesale purchases of energy that were not needed or unduly expensive. The MPSC has not determined whether less expensive alternatives were available to MP&L, but would, as part of its prudency review, examine this matter in detail.[10] Appellant and *amici* for the Federal government and FERC have attempted to refute the finding by the Mississippi Supreme Court that MP&L overlooked ample, less expensive power when purchasing Grand Gulf energy by attempting to focus on the alleged integrated structure of the Middle South system. Appellant's Brief, at 4-5; U.S./FERC Brief, at 14-15. Moreover, they conveniently ignore the fact that no limiting entitlement agreement exists here as was the

10 Contrary to the assertion of *amici* U.S./FERC, this type of review was clearly contemplated by the Mississippi Supreme Court. U.S./FERC Brief, at p. 22, n. 12. A close reading of the entire paragraph shows that the Court was concerned about prudency of the generating plant investment, the generation costs to be reflected in retail rates, and actions taken or not taken by MP&L and Middle South Utilities in light of dramatic changes in retail electric demand and substantial increases in project costs. J.S.App. 9a, 15a-16a.

case in *Nantahala, supra*.

Despite these arguments, however, the Court may determine that a satisfactory record as to the availability to MP&L of other quantities of energy has not yet been developed. If so, the Court should remand the case and require the MPSC to supplement the record by conducting a prudency review and determine whether less expensive energy sources were available to MP&L.[11]

CONCLUSION

For the reasons stated above, the Mississippi Supreme Court's Order should be affirmed and the MPSC allowed to review the prudence of MP&L's decision to participate in a wholesale transaction before imposing the costs of that transaction on retail ratepayers. In the alternative, the Court should remand this action for final determination by the MPSC of the

11 NASUCA disagrees with the U.S./FERC contention that the Mississippi Supreme Court has finally decided the question of MP&L's right to recover substantial Grand Gulf expenses. U.S./FERC Brief, at p. 14. No such order has been issued. *See*, U.S./FERC Brief, at p. 12.

availability of less expensive supply alternatives to meet the energy needs of MP&L.

Respectfully submitted,

STEVEN W. HAMM*
Consumer Advocate of South Carolina and Chairman of NASUCA's Electric Committee

RAYMON E. LARK, JR.
Assistant Consumer Advocate of South Carolina and Member of NASUCA's Electric Committee

National Association of State Utility Consumer Advocates
2801 Devine Street
Post Office Box 5757
Columbia, SC 29250
(803) 734-9464

ELIZABETH ELLIOT
Ass't Staff Counsel for Nevada Attorney General's Office of Advocate for Customers of Public Utilities, NASUCA Members

Dated January 22, 1988

---

* Counsel of Record

See Kentucky West case cited at 15. This case was affirmed after the printing of this Brief in No. 87-5052 (3d Cir. Jan. 19, 1988).

AMICUS CURIAE

BRIEF

(15)

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER AND LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI *ex rel.*
EDWIN LLOYD PITTMAN, Attorney General, and
THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF OF THE NATIONAL GOVERNORS' ASSOCIATION, NATIONAL ASSOCIATION OF COUNTIES, INTERNATIONAL CITY MANAGEMENT ASSOCIATION, U.S. CONFERENCE OF MAYORS, AND NATIONAL LEAGUE OF CITIES AS *AMICI CURIAE* IN SUPPORT OF APPELLEES

ROBERT H. LOEFFLER
MARGARET A. FLAHERTY
MORRISON & FOERSTER
2000 Pennsylvania Ave., N.W.
Suite 5500
Washington, D.C. 20006
(202) 887-1500
Of Counsel

BENNA RUTH SOLOMON
Chief Counsel
STATE AND LOCAL
LEGAL CENTER
444 N. Capitol Street N.W.
Suite 349
Washington, D.C. 20001
(202) 638-1445
Counsel of Record for the
Amici Curiae

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED

Whether a State's authority to determine the prudence of the construction of a generating facility, in setting rates for retail electric customers, is preempted by a decision of the Federal Energy Regulatory Commission allocating the cost of construction among affiliated utilities in three States.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES Page

TABLE OF AUTHORITIES—Continued

ADMINISTRATIVE DECISIONS Page

STATUTES

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER AND LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI *ex rel.*
EDWIN LLOYD PITTMAN, Attorney General, and
THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF OF THE NATIONAL GOVERNORS' ASSOCIATION, NATIONAL ASSOCIATION OF COUNTIES, INTERNATIONAL CITY MANAGEMENT ASSOCIATION, U.S. CONFERENCE OF MAYORS, AND NATIONAL LEAGUE OF CITIES AS *AMICI CURIAE* IN SUPPORT OF APPELLEES

INTEREST OF THE *AMICI CURIAE*

The *amici*, organizations whose members include state, county, and municipal governments and officials throughout the United States, have a compelling interest in legal issues that affect the powers and responsibilities of state and local governments.

Amici are concerned because this case illustrates the increasing tendency of businesses to avoid state regulation in areas of traditional state authority by invoking federal supremacy and the more sympathetic forum of federal regulatory agencies. In 1974, Mississippi Power & Light Company ("MP&L") and Middle South Energy, Inc. obtained a certificate of public convenience and necessity from the Mississippi Public Service Commission ("MPSC") to construct Grand Gulf, a two-unit nuclear power plant, scheduled for completion in 1980 at an estimated cost of $1.227 billion. The proposed construction was a project of Middle South Utilities ("MSU"), a holding company that is the sole stockholder of MP&L, Arkansas Power & Light Company, Louisiana Power & Light Company, and New Orleans Public Service, Inc. Only one of the two units was ever constructed. It cost $3.5 billion, almost $2.3 billion more than the projected cost of both.

In 1982, two separate proceedings were instituted before the Federal Energy Regulatory Commission ("FERC") to obtain review of two MSU system agreements, which included the allocation of costs for Grand Gulf. Two and one-half years of hearings produced two different decisions by two Administrative Law Judges; the one that FERC adopted allocated 33% of the total cost of Grand Gulf to MP&L. MP&L now contends that MPSC must uncritically pass through to the retail ratepayers of Mississippi the entire amount of that 33% share. Automatic pass-through would ignore the enormous increase in the estimated cost which furnished the basis of the original MPSC certificate; the change in the originally proposed allocation of that cost; the delay in completion; the intervening acquisition of additional capacity by MP&L; and the reversal of an anticipated increase in demand for power. In short, Mississippi ratepayers must pay for power that they do not need simply

to meet the cost of a "catastrophically uneconomical" investment.[1]

FERC asserted jurisdiction based on the interstate corporate structure of MSU; the holding company "sells" Grand Gulf power to its affiliates at wholesale. Appellant and its *amici*, including FERC, have told this Court that state and local public utility commissions may not, in exercising their authority to determine the appropriate *retail* rate base, question the prudence of the decision to proceed with the construction of Grand Gulf because it would interfere with the federal jurisdiction over *wholesale* sales. In effect, the federal authority, which was created to fill a regulatory gap resulting from constitutional restrictions on the States' power over interstate energy transactions, is said to strip the States of any effective authority in their traditional area of responsibility, which Congress intended to preserve. The State's interest in this case is not (as it was in *Nantahala Power & Light Co. v. Thornburg*, 106 S.Ct. 2349 (1986)) to challenge the FERC's *allocation* of cost among MSU's subsidiaries, but, rather, to determine whether all of that cost was prudently incurred, a question that FERC never resolved, nor even thoughtfully considered.

If this Court should reverse the judgment of the Mississippi Supreme Court, local utility rate regulation would become dependent on consent. Any utility could avoid state regulation by the simple expedient of affiliating with a wholesaler, and thereby place its rate base within the exclusive jurisdiction of FERC, an agency without any knowledge of local conditions and needs. Instead of filling a regulatory gap, the congressional plan for regulation of wholesale energy rates would become a forum-shopping device. Because this Court's de-

---

[1] *Mississippi Industries v. FERC*, 808 F.2d 1525, 1528, *modified on rehearing*, 822 F.2d 1104 (D.C. Cir.), *cert. denied*, Nos. 86-1380, 86-1424, 87-469 (Dec. 14, 1987).

cision will have a direct effect on matters of utmost importance to *amici* and their members, *amici* submit this brief to assist the Court in its resolution of the case.[2]

STATEMENT OF THE CASE

Although a lengthy factual presentation is not necessary here, a summary discussion of the circumstances under which this case arises will help to explain the conflict between the intent of Congress expressed in the Federal Power Act, 16 U.S.C. §§ 791a-828c ("FPA" or "the Act"), and the assertions of preemption in this case.

In 1974, Mississippi Power & Light Co. ("MP&L") and Middle South Energy, Inc. ("MSEI")[3] petitioned the Mississippi Public Service Commission ("MPSC") for a Certificate of Convenience and Necessity to construct "a two-unit nuclear-fueled electric generating plant" ("Grand Gulf") in Port Gibson, Mississippi. Motion to Dismiss App. 1. In their application, MP&L and MSEI represented that construction of Grand Gulf was in the public interest, that it was necessary to meet the projected demand for power in Mississippi and surrounding States, and that the cost of constructing the two units would be approximately $1.2 billion. *Id.* at 13-15. MP&L's inability to finance the project alone was an issue in that proceeding. MP&L and MSEI represented that MSEI would finance the project, but that MP&L would be in charge of the "design, construction, maintenance and operation" of the project. *Id.* at 31-32. On the basis of these representations, the MPSC issued a Certificate of Convenience and Necessity to MP&L and

[2] Pursuant to Rule 36 of the Rules of this Court, the parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

[3] The brief refers to MSEI, although it has been succeeded by System Energy Resources, Inc.

MSEI on May 29, 1974, to construct Grand Gulf. The Certificate incorporated all of the representations in MP&L and MSEI's petition.

The reduced load growth forecasts in the 1970s for the Middle South System soon made clear that the capacity that would be available from Grand Gulf was not needed to meet the demand forecast in the application to the MPSC. *Middle South Energy, Inc.*, 26 FERC (CCH) ¶ 63,044, at 65,103 (1984). The original plan called for the first unit to become operational in 1980. J.S. App. 13a. In 1979, construction of the second unit was suspended (*id.* at 79a n.2), and it has not been resumed. By 1982, the total cost projected for Grand Gulf exceeded the original estimate by 400%, or $4 billion. 26 FERC at 65,103. Grand Gulf 1 was completed on July 1, 1985, at a cost in excess of $3.5 billion (J.S. App. at 13a); it came on line at a cost per kilowatt of $2,933 (Brief for Appellant 8-9 n.9), four to five times greater than the cost of any existing unit on the MSU system. J.S. App. 16a.[4]

On November 16, 1984, MP&L filed with the MPSC an application for a retail rate increase to obtain the revenues to pay for increased costs of operation due to inflation, a new electric power station,[5] and Grand Gulf 1 construction costs. *Id.* at 8a. Although the MPSC was initially reluctant to allow pass-through of the Grand

[4] Even under the most optimistic assumptions, through 1992 Grand Gulf power would cost ratepayers $3 billion more than power generated from existing alternative units on the Middle South system. The "crossover" point (the time when Grand Gulf would begin costing less than other alternatives) was predicted to be 1993. The "make whole" point (the time at which ratepayers will have recouped past excess payments) will not occur until the 21st century. 26 FERC at 65,103.

[5] While Grand Gulf was under construction, MP&L purchased an interest in a coal-burning generating unit (ISES2) in Arkansas. J.S. App. 8a-9a.

Gulf costs, full recovery was finally approved, largely to mitigate MP&L's deteriorating financial situation. *Id.* at 12a. The increase of almost $3.2 billion was phased in over a ten-year period so that consumers would pay less than the full amount during an initial period and gradually pay the difference (plus financing charges) over a later period. *Id.* at 10a-11a.

The Mississippi Supreme Court reversed the MPSC's order permitting a gradual pass-through of Grand Gulf 1 costs. The court ordered the MPSC to investigate whether MP&L and MSEI acted prudently when they continued construction of Grand Gulf 1 "in light of the change in demand for electric power" in Mississippi and the steep "escalation of costs" that attended its construction. *Id.* at 19a-20a.

SUMMARY OF ARGUMENT

This case arises from Congress's division of jurisdiction over electric power sales between the federal government and the States more than fifty years ago in the Federal Power Act ("FPA" or "the Act"). In this case, the Federal Energy Regulatory Commission ("FERC") relied upon its exclusive jurisdiction over wholesale sales in interstate commerce to allocate among the subsidiaries of a multi-state holding company the cost of constructing a nuclear energy generating facility. Appellant asserts that FERC's allocation preempts Mississippi's authority, in connection with its retail rate-setting function, to determine the prudence of the costs incurred in the construction of the generating facility, even though FERC undertook no such determination, and, indeed, is limited by the Act's explicit provision that the Commission "shall not have jurisdiction" over generating facilities (16 U.S.C. § 824(b)(1)). In effect, appellant asks this Court to disregard the plain language of the FPA to find implied preemption of the States' statutory jurisdiction over generating facilities.

This Court's well-settled preemption doctrines do not support appellant's position. The statute itself, far from expressing any intent to preempt or to occupy the field of electric power regulation, reflects Congress's deliberate choice of dual federal-state regulation in this area. There is no showing that any statutory purpose would be undermined by the State's prudence review. That FERC may not achieve through preemption the regulation of generating facilities, which Congress has explicitly withdrawn from its jurisdiction, is demonstrated by this Court's recent decision under a comparable provision of the Communications Act. *Louisiana Public Service Comm'n v. FCC*, 106 S.Ct. 1890 (1986).

This Court's decision in *Nantahala Power & Light Co. v. Thornburg*, 106 S.Ct. 2349 (1986), does not bridge the gap between the asserted preemption of MPSC's authority and the express language and statutory purpose of the FPA. *Nantahala* ruled that a State, in setting retail rates, must "give effect" to FCC-approved wholesale rates for purchased power. In that case, the rate established by FERC depended upon allocation of the only sources of power available to the company; the State's attempt to change that allocation would have denied the company the ability to recover prudently incurred costs. Here, by contrast, Mississippi does not seek to review the allocation made by FERC, but simply to determine whether MP&L acted prudently in constructing the facility.

Affirmance of the judgment below will honor the "bright line" (*FPC v. Southern California Edison Co.*, 376 U.S. 205, 215 (1964)) drawn by Congress between federal and state jurisdiction that left regulation of generating facilities on the state side of that line.

ARGUMENT

I. FERC'S JURISDICTION UNDER THE FEDERAL POWER ACT DOES NOT PREEMPT THE STATES FROM DETERMINING THE PRUDENCE OF THE CONSTRUCTION OF GENERATING FACILITIES.

The Federal Power Act was enacted in the wake of *Public Utilities Comm'n v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927), which held that the States lacked jurisdiction to regulate rates for the sale of electricity beyond their borders. The *Attleboro* ruling created a regulatory gap, which Congress set out to close in the FPA by giving the Federal Power Commission ("FPC"), FERC's predecessor, jurisdiction to regulate sales of electric energy at wholesale in interstate commerce. 16 U.S.C. § 824(b)(1); *see Arkansas Electric Cooperative Corp. v. Arkansas Public Service Comm'n*, 461 U.S. 375, 378-79 (1983).

FERC based its jurisdiction to allocate a certain percentage of the costs of Grand Gulf to MP&L on that authority. FERC did not examine the prudence of the decision to construct Grand Gulf or whether that construction was economically undertaken and accomplished.[6] In fact, the FPA does not assign that decision to FERC. The FPA specifically provides that the FPC "shall not have jurisdiction, except as specifically provided . . . over facilities used for the generation of electric energy or over facilities used in local distribution." 16 U.S.C. § 824 (b)(1).

MP&L and FERC nevertheless argue that where affiliated public utilities in several States combine for purposes of planning generating capacity and purchasing power at wholesale, and FERC has, in the context of setting a just and reasonable wholesale rate, allocated among them the costs of constructing a generating plant, the FPA preempts the States' traditional power to consider whether the construction of the facility was prudently and economically undertaken and accomplished.

[6] MP&L (Brief at 13-14 n.13) and FERC (Brief at 19 n.10) contend that FERC, in effect, considered the prudence of Grand Gulf construction costs. The record makes clear, however, that although the Administrative Law Judge (ALJ Liebman) and the parties to the administrative proceeding may have mentioned the prudence issue from time to time, it was neither actively litigated nor resolved. See 26 FERC (CCH) ¶ 63,044, at 65,112-13.

This Court's preemption cases do not support this argument. Congressional intent is the touchstone of preemption analysis (*California Federal Savings & Loan Ass'n v. Guerra*, 107 S.Ct. 683, 689 (1987)); and this Court has made clear time after time that it "starts with the basic assumption that Congress did not intend to displace state law." *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981). A finding of preemption must rest on express statutory language or a statutory framework that occupies the regulatory field (*see Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977); *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)); or on a conflict between state law and federal law, either because compliance with both "is a physical impossibility" (*Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142-43 (1963)), or because state law "stands as an obstacle to the accomplishment and execution of the full purposes and objective of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941). None of the requirements for preemption is satisfied in this case.

Express preemption. The FPA does not expressly preempt state regulation of generating facilities; in fact, it expressly denies to FERC jurisdiction over those facilities. To read the Act as depriving the States of jurisdiction over those facilities would attribute to Congress the intent to create a new regulatory gap in a statute purposefully designed to close an old one.

Occupation of the field. Neither does the FPA occupy the field of regulating electric power. On the contrary, the legislative history demonstrates that Congress en-

visioned a system of dual, complementary state and federal regulation.

> "The bill takes no authority from State commissions and contains provisions authorizing the Federal Commission to aid the State commissions in their efforts to ascertain and fix reasonable charges. . . . The new parts are so drawn as to be a complement to and in no sense a usurpation of State regulatory authority and contain throughout directions to the Federal Power Commission to receive and consider the views of State commissions. . . . As in the Senate bill no jurisdiction is given over local distribution of electric energy, and the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State."

H.R. Rep. No. 1318, 74th Cong., 1st Sess. 7, 8, 27, *quoted in Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 526-27 (1945).

In particular, Section 824(b) was intended to preserve to the States one of the most important functions traditionally associated with their police power. *Arkansas Electric*, 461 U.S. at 377. This Court has repeatedly recognized that public utilities are subject to the oversight and control of local authorities. *See, e.g., Central Hudson Gas & Electric Corp. v. Public Service Comm'n of New York*, 447 U.S. 557, 569 (1980); *Frost v. Corporation Comm'n*, 278 U.S. 515, 534 (1929). Local regulation serves, among other values, political accountability for decisions that have public impact. *See Munn v. Illinois*, 94 U.S. 113, 130-33 (1877). Even where the federal government seeks to advance other values, such as the development of nuclear energy under the Atomic Energy Act, "States retain their traditional responsibility in the field of regulating electrical utilities for determining questions of need, reliability, cost, and other related state concerns." *Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Comm'n*, 461 U.S. 190, 205 (1983).

Actual conflict. Appellant has demonstrated no actual conflict between FERC's jurisdiction over wholesale rates and the State's traditional authority to examine prudence in determining retail rates.[7] The FPA is premised on a system of dual regulation; no constitutionally prohibited conflict can arise from the mere fact of state regulation in an area that is also federally regulated where Congress has expressly preserved the state role.[8] Because Congress did not choose to create a unitary scheme of regulation, it was apparently willing to tolerate the problems that normally arise between two regulatory masters.[9]

---

[7] There is not even hypothetical conflict unless it is assumed that MPSC will go beyond the prudence review ordered by the Mississippi Supreme Court.

[8] In *Connecticut Light*, this Court noted not only that Congress may prefer a dual regulatory system over efficiency, but also the important federal goals served by state regulation:

> [S]tate lines and boundaries cut across and subdivide what scientifically or economically viewed may be a single enterprise. Congress is acutely aware of the existence and vitality of . . . state governments. It sometimes is moved to respect state rights and local institutions even when some degree of efficiency of a federal plan is thereby sacrificed. Congress may think it expedient to avoid clashes between state and federal officials in administering an act such as we have here. . . . Congress may think complete centralization of control of the electric industry likely to overtax administrative capacity of a federal commission. It may, too, think it wise to keep the hand of state regulatory bodies in this business, for the "insulated chambers of the states" are still laboratories where many lessons in regulation may be learned by trial and error on a small scale without involving a whole national industry in every experiment.

Connecticut Light, 324 U.S. at 530-31.

[9] There is ample evidence that Congress will authorize preemption of state regulatory authority over local electric utilities when it intends FERC to have the power to preempt. For example, the Public Utilities Regulatory Policies Act, 16 U.S.C. § 824a-1, companion legislation to the FPA, expressly allows FERC to preempt

Congressional purpose. Finally, appellant has not shown that the States' exercise of their traditional function of reviewing prudence in setting retail rates will frustrate federal purposes. One of the primary purposes of the FPA was to preserve the States' jurisdiction over facilities used for the generation of electric energy and facilities used in local distribution. 16 U.S.C. § 824(b). Another was to fill the regulatory gap that existed at the wholesale level while interfering as little as possible with traditional state regulatory authority at the retail level. Neither of these purposes requires preemption in this case; in fact, preemption would disserve Congress's purposes.

Only one statutory purpose has been identified that might be frustrated by the MPSC's prudence review: FERC's responsibility to set wholesale rates.[10] Appellant asserts, essentially, that FERC will be unable to perform its task unless the States are preempted from performing theirs.

This type of argument has been made to this Court before, and has been unsuccessful. In *Louisiana Public Service Comm'n v. FCC*, 106 S.Ct. 1890 (1986), the Court considered the dual regulatory scheme established under the Communications Act of 1934, 47 U.S.C. § 151 *et seq.*, and in particular the Act's grant of authority to the FCC to regulate "interstate and foreign commerce in wire and radio communications" (47 U.S.C. § 151), while expressly denying that agency "jurisdiction with respect to . . . intrastate service." 47 U.S.C. § 152(b). There, the industry and the federal agency made the argument made here: that state regulation would frustrate federal purposes. The Court rejected that argument in construing a statute identical to the FPA in its delineation of separate spheres of state and federal authority. *Louisiana PSC* held that the FCC lacked the authority to require the States, in setting intrastate telephone rates, to use the federal depreciation formulas used in setting interstate rates.[11] The Court recognized that a broad reading of the federal purposes in Section 151 might support the inference that state regulation that frustrates the ability of the FCC to perform its statutory functions was barred. *Id.* at 1899. The Court held, however, that the "express jurisdictional limitation" imposed by Section 152(b) precluded this broad reading. Where the statutory scheme explicitly denied federal power, there could be no preemption based on frustration of federal purposes. *Id.*[12]

This Court has held that 16 U.S.C. § 824(b)(1), the section at issue here, imposes a jurisdictional limitation on federal authority. *Connecticut Light & Power Co.* considered the effect of the denial of FPC jurisdiction "over facilities used for the generation of electric energy or over facilities used in local distribution." The Court held

---

the States' authority to prohibit local distribution companies from entering into pooling agreements.

[10] MSU's purpose of recovering the entire amount of a "catastrophically uneconomical" investment (*Mississippi Industries v. FERC*, 808 F.2d 1525, 1528, *modified on rehearing*, 822 F.2d 1104 (D.C. Cir.), *cert. denied*, Nos. 86-1380, 86-1424, 87-469 (Dec. 14, 1987)) is obviously not a purpose of the FPA; and its frustration, if that is the result of Mississippi's prudence review, does not rise to constitutional proportions under the Supremacy Clause.

[11] The Court specifically rejected the argument that state regulation would frustrate federal purposes because the same plant could be used interchangeably to provide interstate and intrastate service. 106 S.Ct. at 1901.

[12] In words that could have been written for this case, the Court said (106 S.Ct. 1901-02):

> [W]e simply cannot accept an argument that the FCC may nevertheless take action which it thinks will best effectuate a federal policy. An agency may not confer power upon itself. To permit an agency to expand its power in the face of a congressional limitation on its jurisdiction would be to grant to the agency power to override Congress. This we are both unwilling and unable to do.

that federal jurisdiction over local distribution companies would not be sustained even though federal purposes might be served by FPC regulation. The Court observed:

> It is hard for us to believe that Congress meant us to read "shall have jurisdiction" where it had carefully written "but shall not have jurisdiction." The command "thou shalt not" is usually rendered as to forbid and we think here it was employed without subtlety or contortion and in its usual sense.

324 U.S. at 528-29. Rather, Congress "meant what it said" by the words "shall not have jurisdiction." *Id.* at 520.[13]

---

[13] In upholding a challenge to FERC's allocation of Grand Gulf costs, the D.C. Circuit concluded that FERC has jurisdiction "where it is found that generation facilities are used as facilities for interstate wholesale sales." *Mississippi Indus.*, 808 F.2d at 1544. According to the court of appeals, "under the clear terms of the statute, [FERC] has been awarded jurisdiction over generating facilities 'to the extent provided in other sections,' including jurisdiction necessary to effectuate regulation of interstate wholesale rates." *Id.* at 1545 n.74. The correctness of these determinations is not before the Court in this case, nor are they relevant to the issue here, which concerns not FERC's jurisdiction over generating facilities for purposes of setting wholesale rates, but the State's jurisdiction over generating facilities for purposes of setting retail rates.

Our reading of *Connecticut Light*, however, precludes, rather than supports, the court of appeals' conclusions. The court's three attempted distinctions of *Connecticut Light* are unpersuasive. First, by definition, a Connecticut local distribution company makes sales only in Connecticut; generating facilities, by contrast, are not defined in terms of the ultimate destination of power generated. Second, the court did not explain why the limitation on federal jurisdiction in the same section of the FPA should not apply equally to generating facilities and local distribution companies. Finally, the "'generating facilities' exception" created by the D.C. Circuit out of footnote 6 of the *Connecticut Light* opinion (324 U.S. at 528 n.6) would nullify the extensive text discussion of the plain meaning of § 824(b)(1), and the holding of the case as well.

At bottom, appellant argues that FERC's preemptive authority may be used to control indirectly what the agency is precluded from regulating directly. The FPA expressly preserves state authority over generating facilities and denies FERC the power to regulate those facilities. If FERC's cost allocation mandates that state regulatory commissions simply pass through costs, without examining whether they were prudently incurred, then it will have effectively ousted the States from their traditional—and statutory—regulatory authority.

Under the FPA, the power to authorize the construction of new generating facilities rests with the States. This authority must include the concomitant right to determine whether that construction is managed prudently and in accord with the conditions of the State-issued certificate of convenience and necessity. Moreover, to construe the FPA as depriving the States of this ancillary authority could have a far more destructive impact on federal jurisdiction and purposes than appellant and FERC attribute to a prudence review by the MPSC. If States lose control over construction costs of generating facilities that they authorize, simply because these facilities serve regional as well as local needs, they will have little incentive to approve the construction of such facilities. Because only the States, and not FERC, can authorize construction of generating facilities, the Nation's power needs may well suffer.

It might be that, were Congress to reconsider the matter today, it would decide to give FERC jurisdiction to regulate construction of generating facilities that will produce power to be shared among several States, and to determine, when a facility is complete, whether all the costs of construction were prudently incurred and may be fully recovered in retail, as well as wholesale, rates. What is at issue here, however, is not what Congress would do today, but what Congress did when it enacted the FPA. Again, *Louisiana PSC* is relevant. In rejecting the good of the telephone industry as

a basis for enlarging federal regulatory authority at the expense of a traditional state function, the Court stated:

> [I]t goes without saying that we do not assess the wisdom of the asserted federal policy of encouraging competition within the telecommunications industry. Nor do we consider whether the FCC should have the authority to enforce, as it sees fit, practices which it believes would best effectuate this purpose. Important as these issues may be, our task is simply to determine where Congress *has* placed the [regulatory] responsibility....

106 S.Ct. at 1893-94 (emphasis in original).

II. *NANTAHALA* DOES NOT REQUIRE PREEMPTION OF STATE JURISDICTION TO REVIEW THE PRUDENCE OF GENERATING FACILITY CONSTRUCTION COSTS.

Appellant and FERC attempt to use this Court's decision in *Nantahala Power & Light Co. v. Thornburg*, 106 S.Ct. 2349 (1986), to bridge the gap between their assertion of preemption and the express statutory language and legislative history. *Nantahala* held that a State may not, in setting retail rates, disallow for purchased power a wholesale price approved by FERC as just and reasonable. Properly construed, this rule is entirely consistent with the FPA's allocation of ratemaking authority between the States and the federal government. *Nantahala* does not control this case. Although the *Nantahala* opinion contains some language that lends support to the assertion of preemption, it must be read in light of the facts before the Court in that case.

Nantahala differs from the present case in two important respects: first, it involved the purchased power component of the retail rate Nantahala was permitted to charge,[14] while this case involves a prudence review of the capital cost component of MP&L's retail rate; second, the state order under review in *Nantahala* conflicted directly with a FERC decision, while here, the Mississippi court did not question the FERC decision as far as it went. The court's concern was something entirely outside FERC's consideration, and, indeed, beyond its jurisdiction: the extent to which MP&L's continued participation in Grand Gulf was consistent with the State's certification of the project and prudent as a management matter. Whatever the MPSC may decide on remand will not affect FERC's determination that one-third of the cost of Grand Gulf should be attributed to MP&L. MPSC is to ensure only that imprudently incurred costs not be imposed on Mississippi's ratepayers.

MP&L wears three hats: it is a wholesale purchaser of electric power from other MSU subsidiaries; it sells electric power at retail to Mississippi consumers; and it is a manager of the construction of a generating facility licensed by Mississippi. Under the express provisions of the FPA, federal jurisdiction encompasses MSU's sales of power and the price that MP&L must pay as a purchaser, and the States are required to give effect to the exercise of federal authority in this area. But federal jurisdiction under the Act does not encompass MP&L's activities as the manager of a generating facility; regulatory authority over that function is preserved to the State. 16 U.S.C. § 824(b)(1). In accordance with the statutory division of authority, FERC did not, in allocating Grand Gulf costs, investigate MP&L's and MSEI's management of the construction of Grand Gulf. The ALJ made clear that his allocation decision was based on the system as it existed in 1982 and that it was for the sole purpose of determining the just and reasonable wholesale rate for the sale of power to MSU's subsidi-

[14] As the opinion carefully pointed out, Nantahala had available only two sources of power: entitlement power and purchased power from TVA. 106 S.Ct. at 2360. FERC determined that the company was entitled to receive only 22.5% of the cheaper entitlement power. Accordingly, North Carolina could not determine that the company "had purchased an unreasonably large quantity of high-cost power from TVA" (*id.*), because FERC had limited the amount of power that it could purchase at the lower "entitlement" rate.

aries.[15] FERC's allocation merely identified each subsidiary's responsibility for system costs; in effect, it sought to assign to each company the responsibility for a "just and reasonable" portion of Grand Gulf's costs. Properly viewed, the federal allocation established a ceiling on each MSU subsidiary's proportional obligation to pay for Grand Gulf costs. It did not, however, establish a floor for MP&L's recovery of costs in its retail rates.

Nantahala supports this distinction between a requirement that a State "give effect" to an existing FERC wholesale rate, when the issue is pass-through of power purchase costs, and a requirement that it defer to aspects of a FERC decision that address matters within the State's jurisdiction. The Court acknowledged the possibility that a state regulatory commission could validly make different findings in a retail rate proceeding than those made by FERC in a wholesale proceeding "with regard to the costs of constructing their facilities." 106 S.Ct. at 2359. Thus, notwithstanding FERC's general findings concerning the control exercised by MSU over its subsidiaries, *Nantahala* would not preclude a finding by the MPSC on remand from the Mississippi Supreme Court that MP&L and MSEI acted independently in matters within their control in managing the construction of Grand Gulf 1, and that they did so imprudently.

To suggest contravention of the FERC order, notwithstanding the separate jurisdictional spheres of FERC and the MPSC, FERC asserts (Brief at 22) that the MPSC has no authority to inquire whether MP&L and MSEI incurred uneconomic and imprudent costs, because if those costs cannot be recovered in its retail rate, they will be shifted to other States, and thus interfere directly with the FERC allocation. Appellant argues that the prudence review will "relitigate the very issues that FERC decided in order to protect in-state economic interests at

[15] The allocation is based on "today's facts and conditions as tempered by what . . . can reasonably [be] expect[ed] in the future." 26 FERC (CCH) ¶ 63,044, at 65,110.

the expense of the interests of citizens in Louisiana, Arkansas, and Missouri." Brief at 45. The decision of MSU subsidiaries outside of Mississippi voluntarily to absorb some portion of Grand Gulf 1 construction costs undermines both arguments.[16] If those settlements do not result in an impermissible shifting of costs, it is difficult to understand how other disallowances in retail rates would. In fact, it is the suggestion that costs *can* be shifted among the States, and not the MPSC's proposed prudence review, that threatens FERC's allocation. That allocation among the States will not be affected by MPSC's determinations.

Finally, the argument that, under *Nantahala*, disallowance of construction costs in Mississippi's retail rate would result in a "trapping of costs" inconsistent with the federal wholesale rate ignores the regulatory status of the costs in this case. The trapped costs referred to in *Nantahala* represented the difference between federal wholesale rates and the wholesale power purchase component of state retail rates. In the present case, the "trapping," if any, does not arise from dishonoring the federal wholesale rate. It arises, if at all, from the exercise of the States' own traditional regulatory authority over generating facilities. Contrary to appellant's suggestion, *Nantahala* did not hold that any less-than-total pass-through of wholesale rates into retail rates is invalid. *Nantahala* recognizes that the "give effect" requirement does not preempt state jurisdiction to inquire into the prudence of a local distribution company's decision to purchase power from a particular source, when it is free to do so, and to disallow purchase

[16] MSU subsidiaries in Arkansas and Louisiana, by voluntary settlement agreements with the public utility commissions, have agreed to absorb substantial portions of Grand Gulf 1 construction costs. *In re Arkansas Power & Light Co.*, Docket No. 85198-U, Arkansas Public Service Commission, "Joint Motion for Approval of a Proposed Settlement Agreement" (Sept. 25, 1985); *In re New Orleans Public Service, Inc.*, Docket No. CD85-1, Resolution R-86-112 (March 20, 1986).

costs that are imprudently incurred because lower cost power is available. *See* 106 S.Ct. at 2360. *Nantahala* also recognized that under the *Narragansett* line of cases (*see Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), *cert. denied*, 435 U.S. 972 (1978)), increased prices may be offset by savings in other areas. 106 S.Ct. at 2357.

In *Nantahala*, this Court concluded that the States may not review the reasonableness of a FERC-approved wholesale rate, but must give it effect as a power *purchase* component of the retail rate. That rule may be necessary to protect the federal wholesale ratemaking authority, which lies on the federal side of the "bright line" drawn by the FPA between federal and state jurisdiction. *FPC v. Southern California Edison Co.*, 376 U.S. 205, 215 (1964). But if the rule is extended to preclude Mississippi's review of the prudence of the *construction* and *management* of a generating facility authorized by the State, it will obliterate that "bright line" and destroy the statutory reservation of the States' traditional authority over generating facilities.

CONCLUSION

For the foregoing reasons, the judgment of the Mississippi Supreme Court should be affirmed.

Respectfully submitted,

ROBERT H. LOEFFLER
MARGARET A. FLAHERTY
MORRISON & FOERSTER
2000 Pennsylvania Ave., N.W.
Suite 5500
Washington, D.C. 20006
(202) 887-1500
Of Counsel

BENNA RUTH SOLOMON
Chief Counsel
STATE AND LOCAL
LEGAL CENTER
444 N. Capitol Street N.W.
Suite 349
Washington, D.C. 20001
(202) 638-1445
Counsel of Record for the
Amici Curiae

January 22, 1988

AMICUS CURIAE

BRIEF

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases:

In the

Supreme Court of the United States

OCTOBER TERM, 1986

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI, *ex rel.* EDWIN LLOYD PITTMAN, ATTORNEY GENERAL and THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF MISSISSIPPI

Brief of Edison Electric Institute as *Amicus Curiae* in Support of Appellant

Interest of *Amicus Curiae* Edison Electric Institute

Edison Electric Institute ("EEI") is the nation's association of investor-owned electric utilities.[1] The members of EEI supply electric service to consumers throughout the United States, serving approximately 96 percent of all customers of investor-owned utilities and 73 percent of this country's electricity users.

Increasingly, the ability to provide electricity on a reliable and economic basis rests upon an array of wholesale for resale and transmission power transactions among EEI's members. In large part, these transactions take place pursuant to the terms of power pooling or other highly integrated contractual or corporate arrangements.[1] These wholesale for

[1] Appellant, Mississippi Power & Light Company ("MP&L"), and its operating utility affiliates, Arkansas Power & Light

(*footnote continued on following page*)

resale flows of power extend across every state border in the continental United States, and provide enormous benefits to power consumers.[2]

The establishment and maintenance of a reliable network of power generation, transmission, and distribution facilities to carry out these arrangements is a task that is national in scope and consequence. As this case demonstrates, the events of the past two decades, mostly national in origin and consequences, have placed great stress on the financing and operation of that network and on the pricing of the services which it provides. Examples of those national events include the rapid inflation of construction and financing costs for major capital projects, the federal government's initiative for the construction of nuclear projects, the dramatic fluctuations in the availability and prices of oil and gas, the governmental and non-governmental efforts to shift from oil-fired and gas-fired electric generation to nuclear and coal-fired electric generation in response to the Arab oil embargo and OPEC pricing actions, the related federal legislation precluding for a time continued reliance upon natural gas for electric generation (see, *e.g.*, the Power Plant and Industrial Fuel Use Act of 1978, 42 U.S.C. § 8301 *et seq.*), the changes in regulatory requirements following the 1979 Three Mile Island accident and the resulting increases in construction and operating costs, and the roller-coaster rapid surges and declines in electric load growth forecasts and usage.

(footnote continued from preceding page)

Company, Louisiana Power & Light Company, New Orleans Public Service, Inc., System Energy Resources, Inc., formerly known as Middle South Energy, Inc. ("MSE"), the owner of a 90% interest in Grand Gulf Station Unit No. 1 which is the subject of this proceeding, and their common parent, Middle South Utilities, Inc. ("MSU"), constitute "a highly integrated and coordinated electric utility system" (R.104a) and are members of EEI.

[2] The Department of Energy's Report, dated March 1987, to the President entitled "Energy Security", states (at 158) that wholesale power transactions have grown by 40% and wheeling by 150% over the past 10 years, while retail sales have grown by only 30%.

The consequence of these national developments has been that nuclear generating capacity placed in service in 1985 (such as the Grand Gulf nuclear generating station which is at the center of this litigation) had an estimated capacity cost on the order of $2,500 per kilowatt (see *Mississippi Industries v. F.E.R.C.*, 808 F.2d 1525, 1531 (n. 15 and n. 17)(D.C. Cir., 1987), or approximately five times the $500 per kilowatt average capacity cost of two nuclear generating units placed in service in 1974 and 1980, respectively, by one of MP&L's affiliates, Arkansas Power & Light Company. This phenomenon is not unique to Grand Gulf or the Middle South System.[3]

As demonstrated by the highly divergent positions of the several states involved in this proceeding, the allocations of costs of a large generating plant or transmission network serving the electric energy needs of customers in several states pursuant to a power pool or other highly integrated contractual or corporate arrangement present issues that in many instances can be resolved only by a neutral federal arbitrator. The rate and other conditions affecting such interstate wholesale power sale and transmission transactions are, therefore, required to be administered exclusively by FERC pursuant to the Federal Power Act. This Court recently emphasized the need to give effect to the preemptive consequences of federal determinations relating to these interstate power operations. *Nantahala Power & Light Co. v. Thornburg*, 106 S. Ct. 2349 (June 17, 1986).

When a utility's costs are "trapped" by conflicting retail and wholesale rate orders, the utility suffers immediate financial repercussions. Its cash flow is disrupted, and its ability to make needed purchases of fuel or power and to

[3] Reports of the Energy Information Administration of the Department of Energy entitled "Nuclear Power Plant Construction Activity" for 1985 and 1986 state (at page 13) that seven nuclear units entered commercial service in 1985 with an average construction cost of $2,466 per kilowatt, eight nuclear units entered commercial service in 1986 with an average construction cost of $2,765 per kilowatt and thirteen nuclear units were expected to enter commercial service in 1987 with an average estimated construction cost of $3,776 per kilowatt.

finance additional capital expenditures is diminished. As in this case, such orders quickly precipitate grave financial crises and threaten to interrupt the operation of wholesale power transactions affecting utilities in several states.

The adverse effects of such financial distress are felt not only by investors in the utility's securities, but by the utility's customers as well. The Mississippi Public Service Commission ("PSC") recognized in this case that, without retail rate relief, MP&L would quickly become insolvent and that, under such circumstances, "future retail service to MP&L's customers is at best uncertain, and at worst inadequate and undependable." (R-38.a) Moreover, such trapping of costs undercuts the commercial certainty required to support wholesale bulk power transactions, interstate interconnections and pooling arrangements. Such transactions and arrangements achieve substantial efficiencies and thus increase the interstate availability of economic and reliable electrical energy.

Part II of the Federal Power Act, 16 U.S.C. § 824 *et seq.*, was enacted in response to the determinations of this Court of the limitation of state authority in the regulation of interstate commerce in electricity. *Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927). The distinction between state and federal jurisdiction under that Act was to be a "bright line," making FERC jurisdiction plenary and extending it to all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the states. *FPC v. Southern Cal. Edison Co.*, 376 U.S. 205, 215 (1964); *Arkansas Electric Coop. v. Arkansas Public Service Commission*, 461 U.S. 375, 379-80 (1983). That "bright line" is in danger of being obliterated by repeated refusals of state commission (and state appellate court) members to accept the Supremacy Clause of Article VI of the Constitution as binding upon them individually. A prompt reminder by this Court that its decisions in *Nantahala* and other cases cited

are controlling in the circumstances here presented would be significant to all of EEI's members, to the millions of customers whom they serve, and to the millions of investors in their securities.

Summary of Argument

The 1987 order of the Mississippi Supreme Court that is the subject of this appeal is wholly inconsistent with the decision of this Court in *Nantahala* issued less than a year earlier. The efforts of the Mississippi Supreme Court to distinguish *Nantahala* have no merit and constitute an impermissible collateral attack on the FERC orders allocating Grand Gulf costs among its interstate wholesale for resale customers including MP&L.

Notwithstanding its characterization to the contrary, that 1987 order of the Mississippi Supreme Court directly and impermissibly challenges FERC's jurisdiction over interstate wholesale rates, the allocations of costs reflected in such rates and the implementing contract arrangements directed by the FERC. Moreover, the Mississippi Court's purported reliance upon a 1932 decision of this Court which antedated the enactment of the Federal Power Act does not withstand analysis.

ARGUMENT

1. There is no merit in the Mississippi Supreme Court's argument that this Court's decision in *Nantalaha* is not controlling in this case.

As Appellant stated in its Jurisdictional Statement,

> [t]he question presented in this case is not only substantial; it is indistinguishable from the issue decided last term in *Nantahala Power & Light Company v. Thornburg*, No. 85-568, 106 S.Ct. 2349 (June 17, 1986).

In *Nantahala*, this Court held that an allocation of "entitlement power" prescribed by FERC in determining a utility's wholesale rates must be given binding effect by the state commission in determining that utility's retail rates. Therefore, the state utility commission's retail rate determination, which was based on a different allocation of "entitlement power", was held to be preempted under the Supremacy Clause by the rate filed with the FERC under Part II of the Federal Power Act (FPA). Accord, *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (1951); *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981).

In reaching its decision in *Nantahala*, this Court approved a body of state court precedent concluding that a state utility commission setting retail rates must allow, as reasonable operating expenses, costs incurred as a result of paying a wholesale rate filed with or approved by the FERC under the FPA, including one case decided by the Mississippi Supreme Court itself, *United Gas Corp. v. Mississippi Public Service Comm'n*, 240 Miss. 405, 127 So.2d 404 (1961). *See also, Narragansett Electric Co. v. Burke*, 381 A.2d 1358 (R.I. 1977), *cert. denied*, 435 U.S. 972 (1978). A preemptive effect attaches to such filed rates in order to preserve FERC's exclusive jurisdiction under the FPA to regulate interstate wholesale rates and arrangements. Otherwise, as *Nantahala* explains (106 S.Ct. at 2359) a utility's wholesale costs could be

"trapped" between the FERC-filed rates the utility must pay, and the state's disallowance of such costs from recovery in retail rates. The decision of the Mississippi Supreme Court catches MP&L's wholesale costs for Grand Gulf power in the trap *Nantahala* condemned. Unless and until the rate schedules allocating Grand Gulf costs) filed in compliance with FERC's decision are modified, they constitute preemptive filed rates which the Supremacy Clause, as applied in *Nantahala*, requires Mississippi's tribunals to recognize.[5]

The Grand Gulf plant became operational on July 1, 1985. The Middle South companies filed the tariffs to implement the FERC 1985 decision and began collecting

[5] In *Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir. 1987), *modified in* 822 F.2d 1104 (D.C. Cir. 1987), petitions for certiorari pending, Nos. 86-1380, 86-1424, and 87-469, the D.C. Circuit unanimously held that FERC's allocation of Grand Gulf costs was within its authority under §§ 205 and 206 of the Federal Power Act to remedy discrimination. In its order of June 24, 1987, granting rehearing, the D.C. Circuit reversed FERC's determination on the merits and remanded for reconsideration FERC's decision to equalize the capacity costs of all nuclear plants in the Middle South system and for an explanation of two other factors. On July 24, 1987, FERC entered an order providing for further proceedings on remand. That order made clear, however, that the rates filed in compliance with FERC's 1985 allocation remain in effect until further action by the Commission on remand:

> The rates currently on file reflect the allocation ordered by the Commission in Opinion No. 234. No other rates being on file or in effect, the rates filed in compliance with Opinion No. 234 remain in effect. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981); *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246 (1951); *see also Burlington Northern Inc. v. United States*, 459 U.S. 131, 141 (1982) ("federal court authority to reject Commission rate orders for whatever reason extends to the orders alone, and not to the rates themselves").

Thus, under the filed rate doctrine, Mississippi tribunals must continue to recognize the current allocation reflected in those rates until they are modified on remand or otherwise as provided in the Federal Power Act.

from MP&L as of July 1, 1985 the amounts called for by such tariffs. Those tariffs are still in effect.[6] Under the filed rate doctrine MSE and MP&L would violate the Federal Power Act if MSE had not collected from MP&L amounts pursuant to the tariffs prescribed by FERC and in effect since July 1, 1985.

The decision of the Supreme Court of Mississippi in this case is a collateral attack on the FERC orders allocating Grand Gulf costs. Those FERC orders were the result of extensive proceedings before the FERC with respect to two agreements among the members of the Middle South System that had been filed with the FERC in 1982. The state public utility commissions, local regulatory agencies, and other public authorities in each jurisdiction served by the Middle South companies (including those in Mississippi) intervened and participated in the FERC proceedings. Each urged a different allocation of Grand Gulf costs. As FERC noted in its June 1985 Order (R-78a),

> . . . despite every encouragement and opportunity, the parties were unable to unanimously resolve their differences.

Thus, FERC was required to serve as the arbiter of the conflicting interstate interests,[7] and to prescribe the allocation

[6] See n.5 *supra*.

[7] In dealing with a comparable challenge by the Public Service Commission of West Virginia to a FERC allocation of the cost burdens of an interstate energy transmission network, the Court of Appeals for the Fourth Circuit recently stated:

> Only FERC, as a central regulatory body, can make the comprehensive public interest determination contemplated by the FPA and achieve the coordinated approach to regulation found necessary in [*Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1972).] . . . . Only FERC has the objectivity and comprehensive overview that transcends these local concerns." *Appalachian Power v. PSC of West Virginia*, 812 F.2d 898, 905 (4th Cir. 1987).

which determined the share of Grand Gulf costs each state would bear. Because the rates reflecting that allocation remain in effect as the only rates on file, *Nantahala* is controlling.

In *Nantahala*, two owners (both subsidiaries of Aluminum Company of America), Nantahala and Tapoco, of a number of hydroelectric projects made available to the Tennessee Valley Authority ("TVA") the output of those projects in return for a constant allocation of low-cost TVA "entitlement power" and the opportunity to buy from TVA more expensive "purchased power." The agreements between Nantahala and Tapoco allocating these two types of TVA power were filed under the FPA. The FERC determined that the allocations between Nantahala and Tapoco should be modified so as to increase modestly the quantity of entitlement power available to Nantahala and directed Nantahala to file with the FERC revised rates to give effect to that decision. Nantahala did so.

The North Carolina Utilities Commission ("NCUC") had contended before the FERC that the FERC should treat Nantahala and Tapoco as a single entity and should allocate the TVA power allocations on that basis, which would have reduced Nantahala's total cost for TVA power substantially more than that resulting from the FERC order. FERC did not do this, because, given the particular history of Tapoco and Nantahala, FERC concluded that it could not find that Tapoco and Nantahala "operate[d] as an integrated system" (*Nantahala*, 106 S.Ct. at 2352).

Nevertheless, NCUC fixed rates for Nantahala's sales to its retail customers on a basis which attributed to Nantahala more low cost "entitlement power" and less higher-cost "purchased power" from TVA than FERC had directed. The North Carolina Supreme Court affirmed the NCUC's action.

On appeal, this Court reversed the North Carolina Supreme Court's decision, holding that the FERC's determination of

the allocation to Nanhatala of low-cost entitlement power was preemptive and that the NCUC's action impermissibly interfered with federal regulation under the FPA.

The basis for federal preemption in this MP&L case is even stronger than in *Nantahala*. After detailed examination, FERC concluded that the Middle South System is a highly integrated system that made critical decisions as a unit and that the allocation of Grand Gulf costs should take that fact into account.

The Mississippi Court's reliance upon the following statement from this Court's opinion in *Nantahala* (106 S.Ct. at 2360) is misplaced:

> Without deciding this issue, we may assume that a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*. (emphasis in original)

But that assumption *arguendo* in *Nantahala* has no applicability here. MP&L did not simply *elect* to purchase the 33% share of Grand Gulf power allocated to it by FERC. Initially, in the Unit Power Sales Agreement ("UPSA") the Middle South companies sought to provide an allocation among themselves of the cost burdens of Grand Gulf which they believed to be appropriate. After extensive and hotly contested proceedings with participation of all interested parties, FERC made a determination allocating the Grand Gulf cost burdens (and associated power entitlements) in the shares which it concluded were most equitable in the light of all the circumstances. That FERC determination increased MP&L's share of Grand Gulf costs to 33% and significantly changed the shares of such costs of the other Middle South operating companies. MP&L has no choice but to bear 33% of the Grand Gulf costs so long as the present MSE tariffs directed by FERC remain in effect—*i.e.*, the quantity and

price of Grand Gulf power to be purchased by MP&L are exactly what FERC directed.

2. The Mississippi Supreme Court's characterization of its decision as not challenging FERC's jurisdiction over interstate rates is far wide of the mark.

FERC's decision stated (R-101a):

> . . . the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent. In other words, the real issue is whether rates among those companies are just, reasonable, and not unduly discriminatory.

Presumably because it recognized that an attempt on its part to do so would have been in blatant disregard of *Nantahala*, the Mississippi Court never explicitly addressed that "real issue" of "whether rates among those [Middle South] companies are just, reasonable, and not unduly discriminatory".[8] But, even though the Mississippi Court stated (R-14a-15a) "we do not challenge FERC's jurisdiction over interstate wholesale rates", the whole of the Mississippi Court's decision is precisely such a challenge—*i.e.*, the Mississippi Court flatly refuses to accept as binding upon it and the Mississippi PSC the FERC allocation of Grand Gulf costs to MP&L.

Moreover, FERC's decision rests in significant part on its conclusion that the Middle South companies constitute a highly coordinated integrated system and that this coordination and integration result in planning, construction and operations which are conducted primarily for the system as a whole (R-104a). But it is precisely those elements of integrated

[8] The "bright line" Congress drew in the Federal Power Act preempts the states from deciding issues over which FERC has asserted its exclusive jurisdiction. See, *e.g.*, *Arkansas, Louisiana Gas Co. v. Hall*, 453 U.S. 571, 580-582 (1981); *Arkansas Electric Coop. v. APSC*, 461 U.S. 375, 379-380 (1983); *FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964).

and coordinated operation and those affiliated relationships that are seized upon by the Mississippi Court (R-16a; R-20a) as justification for its apparent position that the FERC decision allocating Grand Gulf costs may be ignored by the MPSC in determining MP&L's retail rates. Consequently, the Mississippi Court not only challenges the exercise of jurisdiction by FERC, but also the rationale employed by FERC in reaching its conclusion. Both challenges are without merit.

In a similar vein, the Mississippi Court stated that the Unit Power Sales Agreement ("UPSA") (which provides for the sale of Grand Gulf capacity and energy by MSE to three of the Middle South operating companies) does not "fall under the category of FERC approved rates" (R.22a).[9] This bald assertion is simply wrong, as well as directly contrary to the holdings of FERC and the D.C. Circuit that the Grand Gulf UPSA involves rates for the sale for resale of electricity in interstate commerce under the Federal Power Act.

FERC's jurisdiction over the matters here involved is based on Section 206 of the Federal Power Act which provides that, when any rule, regulation, practice or contract affecting a rate, charge or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice or contract to be thereafter observed and in force and shall fix the same by order. FERC stated that the UPSA is "an agreement which 'supplements or supersedes' the coordination arrangements among the MSU utilities and . . . is a contract affecting rates under the 1982 System Agreement (R.167a).[10]

[9] One of the major aspects of the FERC decision was to modify the allocations of such sales among the Middle South operating companies that had been agreed upon by them in the UPSA and to direct corresponding changes in the UPSA and the filing thereof with the FERC.

[10] The District of Columbia panel upheld that analysis, *Mississippi Industries*, 808 F.2d at 1540, and it is not an issue that is the subject of reconsideration on the panel's remand to FERC.

3. The decisions upon which the Mississippi Court purports to rely do not support its position.

The Mississippi Court insists in another part of its opinion (R-21a) that the Mississippi PSC "had the authority, indeed, the duty, to inquire into the prudency" of MP&L's payments to MSE by reason of the rationale of this Court's decision in *Western Distributing Co. v. PSC of Kansas*, 285 U.S. 119 (1932)—a decision which antedated the enactment of the Federal Power Act by more than three years. In that context, the Mississippi Court stated (R-21a):

> We do not read *Nantahala* to the contrary, although it cited with approval several cases involving purchases by closely related entities.

Such a statement is virtually inexplicable.

Nantahala explicitly rests on the "filed rate" doctrine which this Court noted had its genesis for purposes of the Federal Power Act in *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-2 (1951). As summarized in *Nantahala* by this Court, *Montana-Dakota* involved two electric utilities with interlocking directors and joint corporate officers, each of which utilities received some of the other's power at rates that the FPC had determined were reasonable. After separation of the management of the two companies, one brought suit against the other claiming that the rates which it had paid to, and the rates which it had received from, the other were fraudulent and unlawful by reason of the previous interlocking arrangements.

This Court dismissed that claim in *Montana-Dakota*, stating in a portion quoted in *Nantahala* (106 S.Ct., at 2355):

> We hold that the right to a reasonable rate is the right to the rate which the Commission files or fixes, and that, except for review of the Commission's orders, the court can assume no right to a different one on the ground that, in its opinion, it is the only or the more reasonable one.

As the Court pointed out in *Nantahala*, the existence of the interlocking management of the two utilities and the resulting allegations of fraud were irrelevant, again quoting *Montana-Dakota*:

> Perhaps, in the absence of the Commission's approval, such relationship would be sufficient to raise the presumption [of fraud] under state law, but it cannot do so where the federal supervising authority has expressly approved the arrangement.
> *Ibid.*

Moreover, it pointed out that the filed rate doctrine is not a rule of administrative law, but a matter of enforcing the Supremacy Clause.

We submit that the holding in *Western* has been clearly overtaken and replaced by the enactment of the Federal Power Act, the development of the "filed rate" doctrine implementing that Act and the explicit holdings of this Court in *Nantahala* and *Montana-Dakota*.

Similarly, the Mississippi Court's purported reliance upon the portion of the decision in *Appeal of Sinclair Machine Products, Inc.*, 498 A.2d 696, 704 (N.H. 1985), quoted by the Mississippi Court (R.17a), is mistaken.

In that quoted material, the New Hampshire Court explicitly recognized that state regulation of retail electric rates is preempted with respect to matters actually determined by FERC, whether expressly or impliedly. In this case, FERC *expressly* determined the appropriate allocation of Grand Gulf costs among the Middle South companies, including MP&L, and expressly rejected other allocations—including the allocation that MP&L and its affiliates had agreed upon among themselves.

Moreover, *Sinclair* also recognized that, even where matters are not expressly or implicitly resolved by FERC, state regulation is preempted where such state regulation would contradict or undermine FERC determinations or impose inconsistent obligations on the utility companies involved.

On both counts, the Mississippi Court's holding against federal preemption necessarily fails.

The FERC orders obligate MP&L to pay MSE approximately $25 million a month. The record in this proceeding makes it clear that MP&L cannot make such payments to MSE unless MP&L is permitted to charge rates to its customers which make present and/or future provisions for MP&L's obligations to MSE. Specifically, MP&L will be unable to carry out its obligation to make payments to MSE pursuant to the FERC order if its costs of wholesale power are trapped in violation of *Nantahala*.

The Mississippi Court also purports (R-19a) to rely upon the holding of the Fifth Circuit in *New Orleans Public Service Inc.* ("NOPSI") *v. City of New Orleans*, 798 F.2d 858, 862 (5th Cir., 1986) and the application by that court of the abstention doctrine of *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943). But, the Mississippi Court wholly ignores the fact that the last sentence of the material from NOPSI which it quoted stated:

> Nor would federal abstention foreclose the United States Supreme Court from entertaining NOPSI's preemption claim should it wind its way up through the state courts, as is demonstrated by the path of the recent *Nantahala* case.

That is precisely the situation here where, after three years of proceedings before the MPSC and Mississippi courts, MP&L's preemption claim has finally "wound its way" through the state commission and courts to this Court by means of MP&L's appeal. It is also worth underscoring that the *Burford* abstention doctrine is addressed to the lower federal courts, on the express premise that:

> . . . if the state procedure is followed from the Commission to the State Supreme Court, ultimate review of the federal questions is fully preserved here. *Burford*, at 334.

Conclusion

The Federal Power Act expressly preempts state action inconsistent with rates filed pursuant to FERC determinations; this Court has so held recently in *Nantahala* as well as in the past. The insistence of state ratemaking bodies and appellate courts on subordinating national interests to parochial concerns has been made abundantly clear; there can be no doubt as to what the issues are or where responsibility lies for the present unwholesome state of affairs. Only this Court can put an end to this dispute.

Respectfully submitted,

JAMES B. LIBERMAN*
Berlack, Israels & Liberman
1155 Avenue of the Americas
New York, NY 10036
(212) 704-0100
Attorneys for Edison Electric Institute

Of Counsel:
ROBERT L. BAUM
Senior Vice President
and General Counsel
Edison Electric Institute
1111 19th Street, N.W.
Washington, D.C. 20036
(202) 778-6500

December 3, 1987

* Counsel of record.

AMICUS CURIAE

BRIEF

(32)

No. 86-1970

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel. EDWIN LLOYD PITTMAN,
Attorney General of Mississippi and
MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

On Appeal from the Supreme Court of Mississippi

BRIEF FOR THE COUNCIL OF THE CITY OF NEW ORLEANS AS AMICUS CURIAE

OKLA JONES, II
City Attorney
BRUCE E. NACCARI
Assistant City Attorney
BEVERLY ZERVIGON
Deputy Director
Council Utility Regulatory
Office
1300 Perdido Street
New Orleans, Louisiana 70112
(504) 586-4651

WALTER J. WILKERSON
Suite 2720, Poydras Center
650 Poydras Street
New Orleans, Louisiana 70130
(504) 522-4572

CLINTON A. VINCE*
BERNHARDT K. WRUBLE
NANCY A. WODKA
VERNER, LIIPFERT, BERNHARD,
MCPHERSON AND HAND, Chartered
1660 L Street, N.W.
Suite 1000
Washington, D.C. 20036
(202) 775-1000

KENNETH M. CARTER
SIDNEY H. CATES
CARTER & CATES
Suite 1850, Energy Center
New Orleans, Louisiana 70163
(504) 569-2005

Counsel of Record

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

32 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Table of Authorities Continued

Table of Authorities Continued

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 86-1970

MISSISSIPPI POWER & LIGHT COMPANY,
Appellant,

v.

STATE OF MISSISSIPPI ex rel.
EDWIN LLOYD PITTMAN, Attorney General, and
THE MISSISSIPPI LEGAL SERVICES COALITION,
Appellees.

BRIEF FOR THE COUNCIL OF THE CITY OF NEW ORLEANS AS AMICUS CURIAE

STATEMENT OF INTEREST

This brief *amicus curiae* is presented on behalf of the Council of the City of New Orleans (the "Council") by, *inter alia*, its authorized legal officer, in support of appellees. The Council has, under Louisiana law, plenary authority to regulate the retail electric rates charged by New Orleans Public Service Inc. ("NOPSI") to ratepayers in New Orleans.[1] NOPSI, like Mississippi Power & Light Company ("MP&L"),

[1] The Council also regulates the rates charged by NOPSI's sister company, Louisiana Power & Light Company, for service in the Algiers ward of the City of New Orleans.

appellant here, is a wholly-owned subsidiary of Middle South Utilities, Inc. ("MSU") and is a purchaser of electric power from the Grand Gulf 1 nuclear plant owned by System Energy Resources, Inc. ("SERI"), another MSU subsidiary.

Since 1985, the Council has been involved in several retail ratemaking proceedings related to NOPSI's request for increased rates to cover its share of Grand Gulf 1 costs, and in two federal court proceedings in which NOPSI has attempted to prevent the Council from exercising its retail ratemaking functions—including a review of NOPSI's prudence[2] in relation to

---

[2] A prudence inquiry is a traditional ratemaking function, based on the established principle that costs may be passed on to ratepayers only to the extent they are prudently incurred. *Mississippi ex rel. Southwestern Bell Tel. Co. v. Public Service Commission*, 262 U.S. 276 (1923). This reflects the policy that bad business judgment is not the risk of the ratepayers, but the risk of the owners. As articulated in a recent study:

> The concept of a prudent investment in public utility law is a regulatory oversight standard that attempts to serve as a legal basis for judging whether utilities meet their public interest obligations. . . .
>
> * * *
>
> The concept of prudence provides commissions with a principle that does not necessarily require an 'all or nothing' decision in favor of some side, but can allow some sharing of the risks between investors and the ratepayers. The prudent investment test is a tool that regulators are using to provide an answer to the question of who should bear which risks and associated costs.

Burns, Poling, Whitman & Kelly, *The Prudent Investment Test in the 1980s*, The National Regulatory Research Institute (1985) at iv, vi.

the retail rate aspects of its Grand Gulf 1 commitments.[3] The Council has two important concerns here:

First, in seeking reversal of the Mississippi Supreme Court's order, the appellant, and the Federal Energy Regulatory Commission ("FERC") as *amicus curiae*, propose to sweep away all rights of a regulator at the retail level to inquire into the conduct of the electric utility (and, implicitly, to consider rate mod-

---

[3] In the first federal court proceeding, *New Orleans Public Service Inc. v. City of New Orleans*, 782 F.2d 1236, *withdrawn in part*, 798 F.2d 858 (5th Cir. 1986), *cert. denied*, 107 S. Ct. 1910 (1987), (hereinafter, "*NOPSI I*") NOPSI sought an injunction ordering the Council to pass through to ratepayers, immediately, fully, and without exercising traditional regulatory functions, increases that threatened a "severe rate shock effect" on New Orleans. *NOPSI I*, Civ. Act. No. 85-3398, slip op. at 5 (E.D. La., Sept. 16, 1985). That action was dismissed by the district court on the basis of the abstention doctrine. The decision was ultimately affirmed by the Court of Appeals, which rejected the position of the FERC, participating as *amicus*. This Court denied review on April 20, 1987. The retail rate case was settled by an order involving a phase-in plan as well as partial cost absorption by NOPSI to moderate "rate shock". *See* Council Res. No. R-86-112 (Mar. 20, 1986).

In October 1985, the Council instituted an investigation into the prudence of NOPSI's actions with regard to Grand Gulf 1 as part of the retail ratemaking proceeding. NOPSI initiated a second federal court proceeding, first seeking to enjoin the investigation, and then narrowing its complaint to seek only an advance prohibition of certain types of remedies. That case was dismissed in December 1986 on the basis, *inter alia*, of the abstention doctrine and lack of ripeness. The Fifth Circuit affirmed on the ground that the case was not ripe for judicial consideration. *New Orleans Public Service, Inc. v. City of New Orleans*, Civ. Act. No. 85-5273 (E.D. La. dismissed Dec. 19, 1986), *aff'd*, 833 F.2d 583 (5th Cir. 1987). The aforesaid settlement had permitted the Council to continue its prudence inquiry.

eration plans) in determining the extent to which, and when, costs incurred at the wholesale level should be passed on to retail ratepayers. This is an extreme position that would have the Court believe that once the FERC has acted, there is nothing to be considered at the retail level—a belief that, as shown in Point II of Argument, *infra*, is incorrect. The result sought here is so broad that it might adversely affect the Council's ability to discharge its retail regulatory responsibilities, despite significant factual differences between the New Orleans' situation and that presented here, involving MP&L.[4]

Second, appellant's arguments contain major misconceptions with respect to options at the state level and the scope of the FERC Grand Gulf allocation proceeding. This is a delicate area of shared state and federal jurisdiction that involves strong local con-

[4] In New Orleans, the Council put into effect increased retail rates substantially reflecting the costs of Grand Gulf 1 under the phase-in plan contained in the March 1986 settlement. The prudence inquiry was, pursuant to the settlement, allowed to take its own course. Therefore, the prudence inquiry did not result in either a denial of a rate increase or a refund order. No remedy for imprudence, if any, could be imposed unless and until a factual record was developed and an administrative decision rendered. Moreover, the Council specifically recognized the FERC's wholesale rate allocation and stated that the Council would not seek to invalidate any interstate contracts or to have NOPSI pay a rate other than as prescribed by the FERC. (Council Res. No. R-85-636, Oct. 17, 1985.) The prudence inquiry itself has focused on whether NOPSI's management acted prudently in respect to matters and alternatives *not* foreclosed by either the FERC's cost allocation or interstate contracts approved by the FERC.

cerns. Premature review here on an insufficient factual record could have a severe impact on the vitality of state regulation in the future, which is of concern to the Council. There should, instead, be a final decision from the Mississippi administrative and judicial systems. In the interim, the Court can protect the parties here by ordering preservation of the *status quo* pending such a final decision.

Should the Court nevertheless decide to consider the merits of MP&L's appeal now, it is critical that there be no misunderstanding with regard to the nature of FERC's allocation of Grand Gulf costs at the wholesale level and its implications for retail rates. The record before the FERC did not encompass any issues of managemental prudence, and the decision of the FERC did not, and properly could not, determine issues of prudence as to actions that might have been taken at the retail level. Thus, its decision should not be given the sweeping effect sought by the appellant and its *amici*. To do so would radically curtail the authority of retail regulatory bodies and extend that of the FERC, contrary to Congressional intent. This prospect is of major concern to the Council, which has retail regulatory authority under state law.

SUMMARY OF ARGUMENT

This appeal is not ripe for plenary review. The Mississippi Supreme Court order before the Court is not a final decision within the meaning of 28 U.S.C. § 1257(2). The Mississippi court has remanded the case for further action by the MPSC—specifically, to conduct a prudence inquiry, the scope of which is as yet undefined, into MP&L's prudence with regard to Grand Gulf 1. The Mississippi court has suggested certain subjects for review by the MPSC, but there

is no record based on which this Court can determine now whether the state will take any action preempted by the FERC's allocation of Grand Gulf costs at the wholesale level. It cannot be presumed in advance that the MPSC will intrude upon areas of exclusive federal jurisdiction in its review, or that it will fashion any remedy, should it find managemental imprudence, that would conflict with federal law.

Under the procedural model contemplated by *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 106 S. Ct. 2349 (1986), and the Court of Appeals decision that preceded it[5], Mississippi should be permitted to develop a factual record on prudence at the retail level, reach a decision on the merits and fashion appropriate relief, if needed, before plenary review by this Court. Only in that manner can unnecessary federal intrusion into state affairs, as well as speculation in the absence of a factual record, be avoided.

The exceptions to the finality requirement cited by MP&L (*see, e.g., Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975)) do not support consideration of the appeal now. MP&L states that the Mississippi Supreme Court's order causes immediate harm since it requires a "roll back" of MP&L's rates and a refund of amounts collected.[6] However, this Court has

---

[5] *Aluminum Company of North America v. Utilities Commission of the State of North Carolina*, 713 F.2d 1024 (4th Cir. 1983),*cert. denied*, 456 U.S. 1052 (1984).

[6] This, we should note, represents a significant difference between the Mississippi action and that taken by New Orleans. The Council allowed NOPSI's increased rates to go into effect under a settlement agreement, letting the prudence inquiry run its own course, with any adjustment to be made later only if imprudence at the retail level were found.

stayed that part of the Mississippi court's order and can continue the *status quo* pending completion of the MPSC prudence inquiry and subsequent review. Alternatively, the Court could confine its review to that portion of the Mississippi Supreme Court order requiring that a prudence inquiry be held *before* any retail recovery of Grand Gulf costs is allowed—a requirement that had unusual impact here, given the time that has elapsed since the Grand Gulf costs were first allocated to MP&L by the FERC. A decision on the propriety of the scope of the inquiry and relief at the retail level should be deferred until a record is developed in the state system and a final judgment rendered.

The second exception relied upon by MP&L is equally inapplicable. MP&L argues that federal preemption of the state's regulatory rights at the retail level is so complete that the issue can be determined apart from any factual record on prudence issues. However, unlike the cases relied upon by MP&L, where federal preemption was absolute, here the Federal Power Act contemplates a division of regulatory authority between the FERC and the States. Mississippi is not preempted from conducting any retail level prudence inquiry whatsoever. The FERC Administrative Judge presiding over the Grand Gulf hearings refused to consider issues of prudence—particularly the prudence of the MSU operating companies as purchasers of wholesale power at the *retail* level—on the express basis of state regulatory authority. Moreover, the FERC's Acting Chairman testified before Congress that the FERC did *not* consider retail prudence issues here.

This Court's *Nantahala* decision simply does not preclude the states from considering managemental prudence as an element of retail ratemaking. To the contrary, *Nantahala* recognizes the role of retail ratemaking actions given federal regulation of interstate wholesale costs—just as the FERC itself has recognized that rate moderation plans must be fashioned at the state level, notwithstanding federal wholesale allocation. In an appropriate factual situation, the final calculation of retail rates that are based on a FERC-determined wholesale rate may well involve a reduction attributable to acts of mismanagement that either increased costs or failed to secure cost savings.

Even if this Court were to determine that certain avenues of relief are precluded by FERC action, a sweeping rule that precludes the states from exercising any review of management prudence at the retail level is extreme and unwarranted. The public interest in prudent utility management would suffer by such a rule, as would the Congressionally established "bright line" between federal jurisdiction over interstate wholesale matters and local jurisdiction over retail matters.

Finally, there is no evidence in the present record that the Mississippi Supreme Court's order violates the Commerce Clause. No "shifting" of costs to ratepayers in other states has been demonstrated.[7] It

[7] The Council is particularly sensitive to this point because there is testimony in the administrative record before it by NOPSI's own president that cost absorption and rate moderation plans undertaken by other MSU operating companies had *not* shifted costs to ratepayers in other states. Moreover, the Council has itself considered the need not to shift costs, as an element in fashioning any remedy for imprudence.

is entirely plausible that the MPSC could complete its prudence review, and if it found managemental imprudence, fashion a remedy that does not impact ratepayers in other jurisdictions. Moreover, if an operating company owned by a holding company is legitimately charged with the costs of mismanagement, that action does not improperly "shift" costs to another state's residents.

ARGUMENT

I. SINCE THE MISSISSIPPI COURT HAS NOT RENDERED A FINAL DECISION WITHIN THE MEANING OF 28 U.S.C. § 1257(2), THIS APPEAL IS NOT RIPE FOR REVIEW

Final action has not been taken here by the State of Mississippi. Review here of a state court decision is limited to "[f]inal judgments or decrees rendered by the highest court of a State in which a decision could be had. . . ." 28 U.S.C. §1257(2). The state court decision "must be subject to no further review or correction in any other state tribunal; it must also be final as *an effective determination of the litigation* and not of merely interlocutory or intermediate steps therein. It must be the final word of a final court." *Market Street Ry. Co. v. Railroad Commission*, 324 U.S. 548, 551 (1945).[8] (Emphasis added.)

[8] In the context of state court review of an administrative agency decision, the agency order must be the final adjudication in a completed administrative process, and must establish legal rights and relationships to which liabilities or sanctions may attach. Stern, Gressman & Shapiro, *Supreme Court Practice* 135 (6th ed. 1986), citing *Republic Natural Gas Co. v. Oklahoma*, 334 U.S. 62, 69-72(1948); *Laclede Gas Light Co. v. Public Service Commission*, 304 U.S. 398 (1938). Thus, in *Laclede*, where the

No such finality exists here. The Mississippi Supreme Court has remanded the case for further consideration by the MPSC. The MPSC is the only body authorized to frame and conduct a retail prudence hearing at the retail level under Mississippi law, and it has not yet even particularized, much less conducted or completed, its investigation. There is no record on which this Court can determine whether the State actually will take any action preempted by the FERC's allocation or otherwise by federal law.

Review is rendered particularly difficult here because the opinion of the Mississippi Supreme Court is unclear as to the nature of the proposed prudence inquiry, and uses the word "prudence" in several shifting senses and different contexts—including several which vary from normal usage.[9] The court also raises issues which, it suggests, should have been considered by the MPSC in approving MP&L's retail rate increases, but the court's opinion does not establish clear parameters for the agency's review. It cannot be presumed that the MPSC will take action in areas preempted by FERC action in conflict with federal law. "[W]here further proceedings on remand will

Missouri Supreme Court upon review of a Missouri PSC rate order remanded the cause with directions that the commission redetermine certain facts in accordance with the views of the court, the adjudication was not "final." *Id.* at 400.

[9] For example, the Mississippi Supreme Court refers to the "prudency of their [sister MSU companies'] operation" or the "fairness of their many 'in-house' dealings" (J.S. App. 13a); to "a price that is not prudent," (J.S. App. 15a); to the 1982 System Agreement as seeming to be imprudent (J.S.App. 16a); to the prudence of putting the plant on line (J.S. App. 17a); and to the prudence of MP&L's investment in the plant (J.S. App. 19a).

shed additional light on the record, and thereby remove factual ambiguities that preclude an informed judgment on a constitutional issue, there is a compelling reason for concluding that a final judgment has not yet been rendered." Stern, Gressman & Shapiro, *Supreme Court Practice* 129 (6th ed. 1986), citing *Minnick v. California Department of Corrections*, 452 U.S. 105 (1981).

MP&L argues that two exceptions to the "finality" requirement, recognized in *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469 (1975), render review appropriate here. First, MP&L asserts that the state court's judgment should be deemed final since MP&L is threatened with irreparable harm if the Court's stay is lifted and the Mississippi Supreme Court's "roll back"and refund order is allowed to take effect. MP&L Br. at 27-30. Second, MP&L argues that the Mississippi Supreme Court's rejection of its preemption challenge can be considered "wholly separate from and independent of the merits" and that it therefore constitutes a final judgment. *Id.* at 30. Neither of the arguments are valid in the circumstances presented here.

Regarding the issue of interim harm to MP&L, the Court can maintain the *status quo* pending the outcome of the state's prudence inquiry and thus address MP&L's concerns without prematurely limiting the state's ability to act in a delicate area of extreme local concern and divided jurisdiction. The Mississippi Supreme Court order has distinguishable aspects: it not only directed the MPSC to conduct a prudence inquiry, but also held that the state commission "must review the prudency of an investment such as Grand Gulf *before* it can enact rates based on its costs."

(J.S. App. 19a.) (Emphasis added.).[10] This Court could address the problem caused by the latter holding (which had unusual effects here, given the time that has elapsed) without disturbing the court's direction that the MPSC inquire into the issue of MP&L's prudence.

The second argument based on *Cox*—that MP&L's preemption claim can be considered wholly apart from the merits—is inapposite. This exception was described in *Cox* as follows:

> [T]here are those situations where the federal issue has been finally decided in state courts with further proceedings pending in which the party seeking review here might prevail on the merits on nonfederal grounds, thus rendering unnecessary review of the federal issue by this Court, and where reversal of the state court on the federal issue would be *preclusive* of any further litigation on the relevant cause of action *rather than merely controlling the nature and character of*, or determining the admissibility of evidence in, the state proceedings still to come.

420 U.S. at 482-83. (Emphasis added.)

[10] As previously indicated, New Orleans determined to conduct a prudence inquiry, but allowed rates to go into effect pending its completion. The Mississippi court appears to have based its holding on Miss. Code Ann. § 77-3-39. *See* J.S. App. 13a. However, that statute merely requires the MPSC to hold a hearing in every case in which a change in rates is "major" and to *set aside* the rates if they are found to be "unjust, unreasonable or unreasonably discriminatory, or in anywise in violation of the law. . . ." (J.S App. 71a). (Emphasis added).

The cases cited by the Court in *Cox* as exemplifying this proposition[11] pertain to situations in which federal jurisdiction was exclusive or a special federal statute fully determined the issue. Federal jurisdiction is not exclusive here, and no statute authoritatively determines the outcome. Instead, the Federal Power Act contemplates a division of responsibility (often referred to as the "bright line") between the federal government and the states: federal regulation of the sale at wholesale of electric energy in interstate commerce and state regulation of sales at the retail level. *See New England Power Co. v. New Hampshire*, 455 U.S. 331 (1982); *Federal Power Commission v. Southern California Edison Co.*, 376 U.S. 205 (1964).[12] Thus, at most, determination of the federal issue would affect only "the nature and character of . . . the state proceedings still to come" and would not preclude further state action. *Cox*, 420 U.S. at 483. Therefore, there is no basis for an exception to the rule requiring finality.

Mississippi should be permitted to develop a factual record on prudence and to deal with MP&L's position in the context of that record. This is the model fol-

[11] *Construction & General Laborers' Union v. Curry*, 371 U.S. 542 (1963); *Mercantile National Bank v. Langdeau*, 371 U.S. 555 (1963).

[12] In *NOPSI I*, the existence of this "bright line" was pivotal in the Fifth Circuit's view of NOPSI's preemption claim. The court noted that although the company attempted to depict the situation as one in which the retail regulator was attempting to disrupt a federal scheme, it may instead "constitute a disruption of a *state* regulatory scheme, for *retail* ratemaking is clearly a field left to the jurisdiction of the states." *NOPSI I*, 798 F.2d at 860.

lowed in the litigation resulting in *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 106 S. Ct. 2349 (1986).[13] Recently, the Fifth Circuit reaffirmed the appropriateness of this model, rejecting NOPSI's preemption claims with regard to the Council's prudence inquiry on the ground of lack of ripeness. *New Orleans Public Service Inc. v. City of New Orleans*, 833 F.2d 583 (5th Cir. 1987); *see also NOPSI I*, 798 F.2d at 862. Only by allowing the state to develop a final position on MP&L's claims can the Court avoid

[13] MP&L's assertion that the Court applied an "exception" for preemption issues in exercising jurisdiction over "Nantahala III" (*Nantahala Power & Light Co. v. Thornburg*, No. 85-1307, 106 S. Ct. 3268 (June 23, 1986) is erroneous. There was a special basis to vacate *Nantahala III* because it involved the same issues that had just been decided by the Court in *Nantahala I*. Thus, there was no reason to require the state commission to reconsider its rate decision along lines suggested by a direction of the North Carolina Supreme Court's decision, when the substance of decision had just been declared by the Court to be erroneous. No such circumstances apply here.

The appropriate example is, instead, the model of *Nantahala I*. There, the North Carolina Supreme Court directed a remand to the state commission in order to adopt a specific allocation formula then under active review by the FERC. The Court of Appeals refused to intervene, invoking the abstention doctrine, *Aluminum Company of America v. Utilities Commission of the State of North Carolina*, 713 F.2d. 1024 (4th Cir. 1983), *cert. denied*, 456 U.S. 1052 (1984). This Court heard the case only after the matter had been acted upon by the state commission on remand and subsequently reviewed by the state Supreme Court. *State ex rel. Utilities Commission v. Nantahala Power & Light Co.*, 313 N.C.2d 614, 332 S.E.2d 397 (1985). While ultimately disagreeing with the state court, this Court apparently found the state review process to be beneficial, and it complimented the state court for "an admirably thorough consideration of the myriad issues before it." *Nantahala*, 106 S. Ct. at 2354.

unnecessary federal intrusion into state affairs, a basic reason for the final judgment rule. *See North Dakota State Board of Pharmacy v. Snyder's Drug Stores, Inc.*, 414 U.S. 156, 159 (1973); *Radio Station WOW v. Johnson*, 326 U.S. 120, 123-24 (1945).

II. STATE COMMISSION REVIEW OF THE UTILITY'S PRUDENCE IS NOT PREEMPTED BY THE ACTIONS TAKEN BY THE FERC

Relying in part on an erroneous view of this Court's decision in *Nantahala*,[14] and in part on mischaracterization of the FERC's decision in the Grand Gulf case, MP&L asserts that *any* state court review of its prudence in relation to Grand Gulf 1 has been preempted by the FERC's allocation of the Grand Gulf 1 costs among the MSU subsidiaries. It is clear, however, that no considerations of management prudence—particularly prudence from the perspective of the recipient of wholesale power, the focus of the retail

[14] MP&L has attempted to portray the facts of this case as closely aligned to those of *Nantahala* by arguing (*e.g.*, Br. at 3, 12, 24) that the FERC allocated both the high costs of the Grand Gulf 1 power and the low costs of other MSU system power. Apparently, MP&L believes this characterization is akin to the high cost "purchase" power and low cost "entitlement" power which was allocated by the FERC in *Nantahala*. Here, however, a greater allocation of Grand Gulf power for MP&L did not correspondingly reduce the amount of low cost system capacity for which it also would be responsible. Even FERC has acknowledged that "[i]n *Nantahala*, FERC allocated the benefit of low cost power, and in this case FERC allocated the burden of high cost power." FERC Br. at 25 n.17. However, the real issue, not addressed by MP&L's attempt to align the cases, is whether there were cost-saving actions available to the operating company's management in respect to Grand Gulf 1 that it failed to pursue.

regulator—were involved in the FERC's allocation proceeding.

The transcript of the Grand Gulf cost allocation hearings at the FERC plainly indicates that the Presiding Judge refused to be drawn into making indirect or implied rulings on prudence:

> MR. MERRIMAN:
>
> * * *
>
> Now, Middle South Energy is exclusively subject to the jurisdiction of the FERC. It is a 100 percent wholesaler. We don't want somebody later someplace to say that therefore the costs involved in that construction were somehow unjust and unreasonable because you did something wrong.
>
> PRESIDING JUDGE: Okay.
>
> But I can't preclude parties here from somewhere else raising anything they want to raise. And the only thing that I'm concerned about is what matters I should decide. And as far as I can see I don't have to decide the issue of the prudence of the construction—of the decision to construct the Grand Gulf project.

Middle South Energy, Inc., Docket No. ER82-616-000, Transcript of Proceedings, March 14, 1983, at 235-36.

The Presiding Judge was particularly clear that the issue of the prudence of the individual MSU companies as *purchasers* of Grand Gulf power would not be a part of his determination:

> MR. O'SULLIVAN: I just wanted to make sure that there was no confusion between the

> prudence inquiries that I understand you ruled this morning *the states were entitled to make.*
>
> That is, *the prudence of the affiliates* under the jurisdiction of the states making a purchase of Grand Gulf power for purposes of retail resale, and that that issue is not stipulated, the buyers is not stipulated to.
>
> PRESIDING JUDGE: *I'm not getting into that* I don't think in this case.
>
> MR. MERRIMAN: He's not saying one way or the other what the jurisdiction of the state commissions are.
>
> PRESIDING JUDGE: *I'm not getting into that.*

Id. at 228. (Emphasis added.)

At the close of the relevant dialogue, the Presiding Judge said to Mr. Merriman:

> PRESIDING JUDGE: *I don't think you can put me in a position or this Commission in a position of deciding a prudency issue on the allocation issue in such a way that no one can possibly raise this in the State Court.* I think that's the problem you have. I may be wrong.
>
> I don't intend to get into state jurisdiction, but I do intend to get into what a fair and just and reasonable and non-discriminatory rate schedule and agreement is.
>
> MR. EASTLAND: *Wholesale* level.

PRESIDING JUDGE: At the *wholesale* level.[15]

Id. at 248. (Emphasis added.)

In its Opinion Nos. 234 and 234-A,[16] the FERC acknowledged the traditional role of the states in retail ratemaking regulation:

> [W]e concurred in [Judge Head's] discussion of the need to balance Federal and states interests in exercising our jurisdiction. Furthermore, we think our opinion, taken as a whole, as well as Judge Head's discussion, which we adopted, clearly recognize the role of the states in regulating the retail electric rates and the need to balance overlapping state and Federal electric rate jurisdiction.

[15] The FERC's briefs here attempt to portray a reference in Judge Liebman's opinion to a *subjective* belief by the MSU companies' executives that continuing construction of Grand Gulf was prudent as an actual finding by FERC that it was prudent. (FERC Br. at 19 n.10). This would be contrary to accepted law, which requires an objective standard of reasonableness. Additionally, as indicated above, no such findings could have been made by Judge Liebman since he did not consider the issue within the scope of the cost allocation hearing. Should there be any doubt, Judge Liebman's statements can be contrasted with those made in his recent decision in ***Kansas Gas & Electric Co.***, 39 FERC ¶ 63,013 (1987) at pp. 65,058-69, in which prudence clearly was an issue. Moreover, the key prudence issues at the retail level would not necessarily include continuing construction of the plant.

[16] In these opinions, the FERC reviewed Presiding Judge Liebman's decision pertaining to the allocation of Grand Gulf 1 costs, and Judge Head's decision in ***Middle South Energy, Inc.***, 30 FERC ¶ 63,030 (1985), governing the allocation of all generation facilities on the MSU system.

Middle South Energy, Inc., 31 FERC ¶ 61,305 (1985) at p. 61,951. The FERC concluded:

> The basic nature of regulatory control retained by the states under previous System agreements remains unchanged. What our decision attempts to do is amend the filed agreements to achieve a non-discriminatory sharing of excess capacity cost imbalances on the integrated System, consistent with the goal of the System Agreement, and to do so with as little intrusion on the States as possible.

Id. at p. 61,952.

The FERC's Acting Chairman subsequently confirmed in Congressional testimony that the Commission did not determine prudence issues in the Grand Gulf cost allocation hearing. In response to an inquiry as to whether the FERC had considered the prudence of the purchase of Grand Gulf power by the MSU subsidiaries, the FERC Acting Chairman stated:

> The Commission did not determine the prudence of the purchase of power by the Middle South utilities from the Grand Gulf Nuclear Generating Station in Opinion Nos. 234 and 234-A.
>
> At issue in Opinion Nos. 234 and 234-A were the narrower questions of whether the proposed Middle South System Agreement and Grand Gulf Unit Power Sales Agreement allocated the costs of generation and transmission on the Middle South system among its members in a manner that was just, rea-

gemental imprudence present, this Court held that the "filed rate doctrine" prevented the adoption of a contradictory formula and required the states to pass through the wholesale costs in order to avoid their "trapping." 106 S. Ct.at 2359. The Court, however, made it clear that other, traditional retail ratemaking actions (there, the recognition of offsetting costs) could properly be taken into consideration in establishing retail rates, and that their offset against the wholesale rate does not constitute an impermissible "trapping." *Id.* at 2357-58. *See also NOPSI I*, 798 F.2d at 860-61. There may indeed be situations in which a reduction in retail rates based on cost-saving opportunities improperly bypassed by management would be appropriate, even where the wholesale rate has been established by the FERC.

As the very foundation of their argument here, MP&L and the FERC would have this Court believe that once the FERC allocates costs to an electric utility, there is *nothing*—other than the calculation of "cost savings" set forth as an example in *Nantahala*—that the state regulator may do. This is factually erroneous. Moreover, they would have the Court decide this issue in their favor in advance, categorically, and in the abstract, not allowing the state to develop either a factual record or a tailored remedy that might prove otherwise.

There are in fact important inquiries that state regulators may undertake. The problem of "rate shock," for example, must often be addressed by "phase-in" (sometimes called "levelization") plans and other forms of rate impact moderation. These must be left

open for development by local regulators.[18] Otherwise, the full and immediate pass-through of costs championed by the FERC here can become a pyrrhic utility victory, as mounting retail rates destroy the economy of the ratepayer base on which the utility itself relies for survival. Moreover, it is simply not true that because a utility has a commitment to take a source of wholesale power (whether by FERC allocation or "system" assignment), there are no steps a management can take to decrease its risks and lower its costs in the event that commitment proves uneconomic—and these matters bear on the issue of prudent management.[19] Whatever the circumstances in Mississippi,

---

[18] As stated by the administrative law judge in the Grand Gulf 1 case:

> The design of local retail rates to ultimate consumers is a matter within the jurisdiction of the states. . . . Whether a state retail levelization scheme would have the effect of disallowing . . . the wholesale rate . . .[or] would be otherwise illegal are questions which may turn on the *particular* levelization scheme adopted by a state commission. The Federal Energy Regulatory Commission *should not make general pronouncements* now as to whether state levelization plans would be permissible or what kind of retail levelization plans would be permissible for the operating companies of MSU. Abstaining from such pronouncements seems particularly appropriate for FERC in light of the clear bright line . . . between Federal and state jurisdiction over electric utilities.

Middle South Energy, Inc., 26 FERC ¶ 63,030 (1984) at 65,148. (Emphasis added.)

[19] FERC asserts (at p. 22 n.12) that no such inquiry is suggested by the Mississippi Supreme Court's remand to MPSC. As indicated in the preceding section of this brief, the scope of the prudence inquiry required by the Mississippi Supreme Court is unclear on the present record. With deference to the Missis-

there is expert testimony in the New Orleans case that in fact such opportunities *did* exist. The appellant would have the Court decide, as an abstract matter of law and without a record, that such opportunities *could not* exist and that, therefore, no inquiry into this area may be allowed to proceed. This would allow regulated utilities to block the kind of oversight of their management that Congress intended when it maintained the jurisdiction of the states over retail utility matters.

III. UNDERTAKING A PRUDENCE REVIEW DOES NOT VIOLATE THE COMMERCE CLAUSE

MP&L argues that the Mississippi Supreme Court's order violates the Commerce Clause by shifting the burden of its Grand Gulf 1 costs to ratepayers in other states. It contends that the order (1) is invalid *per se* as economic protectionism; and (2) could not survive a balancing test that weighs interference with interstate commerce against legitimate state interests. These contentions are erroneous.

First, certainly the Mississippi court's actions, insofar as it directs the holding of a prudence hearing, cannot be deemed *per se* invalid under the Commerce Clause since there is no indication in the current record[20] that a final prudence decision in Mississippi,

sippi Court, it is not presumed to have expertise in originating administrative prudence investigations. Until the MPSC completes a prudence inquiry and its determination is reviewed by the Mississippi courts, the propriety of that inquiry cannot, in fairness, be reviewed.

[20] Since the stay ordered by this Court is in effect, MP&L is collecting its share of Grand Gulf 1 charges from Mississippi ratepayers. As indicated in an earlier section of this brief, the Court could maintain the *status quo* in Mississippi pending the completion of the MPSC's prudence proceeding and judicial review thereof by the Mississippi courts.

even one that disallows costs, would result in forcing ratepayers in other states to assume a greater share of such costs.[21] It is entirely probable that there is an amount of disallowance that MP&L could bear without significantly affecting its parent or sister companies. As previously indicated, in the New Orleans case there is record testimony by NOPSI's own president that rate absorption and other rate moderations by certain MSU companies did not "shift costs" to other companies in other states.

Second, until Mississippi finally acts in this matter, it is difficult to discern any burden on interstate commerce that could be employed in applying a balancing test—particularly any burden that would outweigh the strong interest in requiring prudent utility management.

The FERC has made a similar error of absolutist argument by contending that "only two sorts of prudence inquiry are logically possible" (FERC Br. at 21)—one which finds the entire MSU system imprudent for undertaking to construct Grand Gulf 1 and requires costs to be borne by MSU's shareholders, and one which determines that Grand Gulf 1 was imprudent for MP&L and requires some or all of MP&L's share to be borne by ratepayers of the other operating subsidiaries. The FERC simply ignores other options

[21] *New England Power Co. v. New Hampshire*, 455 U.S. 331 (1982) is inapposite. There, the state attempted to prevent low-cost hydroelectric power from being sold outside the state, a clear example of economic protectionism with a direct and immediate impact on other states. On the current state of the record here, no such shifting of benefits or burdens has been shown.

familiar to those with experience at the retail level, because MP&L could be found imprudent in respects which do *not* involve plant construction or inter-company allocation, but rather involve risk-management and cost-saving opportunities in power sales arrangements with other companies. Until the MPSC is able to complete its inquiry, and until review of the MPSC's decision is conducted by the Mississippi courts, any argument that the state commission's actions have been preempted or that the Commerce Clause has been violated is both without foundation and premature.

IV. CONCLUSION

For the foregoing reasons, the Council respectfully suggests that the Court dismiss the appeal or postpone decision pending final action by the State, while maintaining the *status quo* by appropriate order. Should the Court decide to consider the appeal, the Court should hold only that the rate roll-back and refund determination was inappropriate in the circumstances of the case, while affirming the right of Mississippi to conduct a prudence inquiry as to retail-level issues.

Respectfully submitted,

OKLA JONES, II
City Attorney
BRUCE E. NACCARI
Assistant City Attorney
BEVERLY ZERVIGON
Deputy Director
Council Utility Regulatory Office
1300 Perdido Street
New Orleans, Louisiana 70112
(504) 586-4651

CLINTON A. VINCE*
BERNHARDT K. WRUBLE
NANCY A. WODKA
VERNER, LIIPFERT, BERNHARD, MCPHERSON AND HAND, Chartered
1660 L Street, N.W.
Suite 1000
Washington, D.C. 20036
(202) 775-1000

*Counsel of Record

WALTER J. WILKERSON
Suite 2720, Poydras Center
650 Poydras Street
New Orleans, Louisiana 70130
(504) 522-4572

KENNETH M. CARTER
SIDNEY H. CATES
CARTER & CATES
Suite 1850, Energy Center
New Orleans, Louisiana 70163
(504) 569-2005

January 22, 1988